4685

IN THE

United States

Circuit Court of Appeals,

FOR THE NINTH CIRCUIT.

Maryland Casualty Company, a Corporation,

Plaintiff in Error,

vs.

The Citizens National Bank of Los Angeles, a Banking Corporation,

Defendant in Error.

BRIEF FOR DEFENDANT IN ERROR.

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Parker, Stone & Baird Co., Law Printers, Los Angeles.

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ERRATA.

Transcript of Record:

Page 431, lines 4 and 5, and page 432, lines 8 and 9, "twenty-nine thousand, three hundred thirty-seven and 99/100 ($29,337.99) dollars" should read: "twenty-nine thousand, three hundred seventy-seven and 99/100 ($29,377.99) dollars."

Brief of Plaintiff in Error:

Page 12, line 11, "ninety-five" should read "ninety-five thousand."

Page 74, line 14, the figures "$29,336.99" should read "$29,377.99."

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Maryland Casualty Company, a Corporation,

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BRIEF FOR DEFENDANT IN ERROR.

Preliminary Statement.

In the brief of the plaintiff in error, at pages 7 to 21, appears what is termed "Statement of Case." It is preceded by: (1) a general statement entitled "History and Nature of the Case;" and (2) a subdivision entitled "Nature of Issues," which appears to be an attempt to state the issues raised by the complaint and answer. The general preliminary facts stated in the first subdivision, entitled "History and Nature of the Case," are somewhat helpful in approaching the matter presented for review. The so-called "Statement

of Case" and "Nature of Issues" are, however, as we view them after careful study and consideration, so entirely insufficient and incomplete as to cause confusion and misunderstanding in the mind of a reader not otherwise familiar with the questions involved and the manner in which they are raised. It is very doubtful if Rule 24 of this court is complied with in this regard; certainly the requirements of the rule are not strictly observed. Accordingly, we shall undertake the unusual burden for a defendant in error of presenting for the court's consideration a concise abstract or statement of the case.

Statement of the Case.

California Cotton & Factorage Company (hereafter called Cotton Company) applied for and the plaintiff in error (hereafter called Bonding Company) executed and delivered to the Cotton Company a fidelity bond agreeing to reimburse it for any loss (not exceeding $50,000.00) of money, securities or other personal property, *including that for which it might be responsible to others,* which it might sustain by reason of any wrongful act of its secretary, J. B. Sears [Tr. pp. 121-125], who acted as general manager, with unrestricted authority to carry on the business affairs of the Cotton Company. [Tr. p. 126.]

The Cotton Company applied for and the defendant in error (hereafter called plaintiff Bank) extended to it a credit account in the amount of approximately $200,000.00. [Tr. pp. 212-215.] The Cotton Company thereupon commenced to purchase cotton at various

points in California and Arizona, arranging for payment by means of sight drafts drawn against the Cotton Company in favor of the vendors and forwarded with cotton tickets (warehouse receipts) attached to the plaintiff Bank. Upon receipt of the sight drafts—cotton tickets attached—they were immediately presented to and accepted by the Cotton Company, acting through Sears [Tr. p. 127], and were then paid by the plaintiff Bank and held by it in its note department as bills receivable, the cotton tickets being attached as collateral. [Tr. p. 127.] Thereafter, ostensibly pursuant to the plan outlined at the time of the application for credit [Tr. pp. 212-215], but in reality, as found by the court, pursuant to a fraudulent scheme then entertained by him, Sears applied for and obtained the cotton tickets from the plaintiff Bank, giving in lieu thereof trust receipts [Tr. pp. 128, 129], then explaining and theretofore having explained [Tr. pp. 212-215] that in the event of a sale of the cotton it would be necessary to surrender the cotton tickets in order to make delivery of the cotton to common carriers for shipment to the purchasers, at the same time obtaining from the common carrier bills of lading which, with the accompanying sight drafts attached, would be returned to the defendant in error and the trust receipts taken up. [Tr. p. 130.]

Instead, however, of keeping his agreement and complying with the terms of the trust certificates, Sears, having sold the cotton and secured bills of lading, presented the same with sight drafts drawn upon the purchasers, to the plaintiff Bank, not, how-

ever, to the note department, but to officers unacquainted with the fact that the cotton covered by the sight drafts was cotton secured by Sears upon the faith of trust receipts then held by the Bank, and then obtained from such officers an O. K. or approval of the sight draft with bill of lading attached, so the same might be deposited as a cash transaction [Tr. pp. 131, 132]; Sears thereupon deposited the draft and attached bill of lading, as a cash item, in the plaintiff Bank to the credit of the Cotton Company, obtained a cash deposit entry in the Bank pass book of the Cotton Company, thereafter caused fraudulent entries to be made in the books of account of the Cotton Company indicating similar credits to its account, and falsified the records and accounts of the Cotton Company by carrying such amounts to the credit of the Company and failing to make any entries indicating the outstanding trust receipts. [Tr. pp. 133, 134.] Sears thereafter represented to the officers of the Cotton Company that he was making money, that the cash items so entered represented profits of the business and that the cotton tickets on hand represented profit. He also represented to the officers of the plaintiff Bank that he had not sold the cotton covered by the trust receipts, that the Cotton Company still had all such cotton tickets and that he could produce them upon demand. [Tr. pp. 134, 135.] In truth and in fact Sears had experienced great financial losses in the business transactions of the Cotton Company and had misapplied the moneys realized from the sale of the cotton covered by trust receipts to

liquidate such losses. [Tr. p. 136.] Sears died May 3, 1921, having committed suicide by shooting himself. [Tr. p. 188.] An audit of his accounts was immediately instituted [Tr. p. 237], which disclosed a shortage largely in excess of the amount of the bond. Notice was immediately given the plaintiff in error as required by the bond [Tr. pp. 237-256]; it denied liability [Tr. p. 267], whereupon an action was instituted by the defendant in error *as assignee* [Tr. p. 365], to enforce the penalty of the bond. Judgment in the amount of $30,101.14 [Tr. p. 166] having been entered against the plaintiff in error, this writ is prosecuted.

PLEADINGS.

Complaint.

In the complaint as amended there was alleged (first cause of action) the identity of the parties [Tr. p. 16], the execution of the bond [Tr. pp. 16-21], the appointment of Sears as secretary of the Cotton Company, his performance of the duties of the office [Tr. pp. 22, 23]; the receipt between November 19, 1920, and April 25, 1921, by the plaintiff Bank of 87 sight drafts totaling $82,487.96, to which were attached 1476 negotiable warehouse receipts, each for one bale of cotton; the acceptance in writing of the sight drafts by the Cotton Company, acting through Sears, the payment of the drafts by plaintiff Bank and the carrying of said accepted drafts upon its books as bills receivable and the warehouse receipts as collateral [Tr. pp. 40, 41]; that immediately following the receipt

of each of the various 87 sight drafts and warehouse receipts and the acceptance thereof by the Cotton Company, Sears on behalf of the Cotton Company applied to and secured from plaintiff Bank said 1476 warehouse receipts, substituting therefor 87 trust receipts under the terms of which, upon the sale of the cotton represented by the warehouse receipts, bills of lading (out-bound documents) covering shipment of the cotton would be returned to the bank in cancellation of the receipts [Tr. pp. 42, 43]; that Sears represented to the officers of plaintiff Bank that the sale of the cotton covered by the warehouse receipts necessitated the surrender of the warehouse receipts in order to obtain possession of the cotton for delivery of the same to common carriers for shipment, and that upon such exchange he would immediately return the bills of lading to the plaintiff Bank and take up the trust receipts. [Tr. pp. 43, 44.] That Sears, pursuant to a fraudulent scheme entertained by him, misappropriated and misapplied 1091 of said 1476 warehouse receipts and 1091 bales of cotton represented thereby, in the following manner: Having secured the warehouse receipts from defendant in error and given trust receipts therefor, Sears, acting as secretary of the Cotton Company, sold the cotton represented by the warehouse receipts and received bills of lading therefor and in violation of the terms of the trust receipts and his promises to the plaintiff, attached said bills of lading to sight drafts drawn against the purchasers of the cotton, presented the sight drafts with bills of lading attached to an officer of plaintiff Bank other

than the officer in charge of the note department, from which the warehouse receipts had been taken, and where the trust receipts had been deposited by Sears, and secured from said officer an O. K. or approval of the sight drafts with bills of lading attached, which enabled Sears to deposit the sight drafts to the credit of the Cotton Company as a cash item. That Sears thereupon deposited said O. K.'d or approved sight drafts with bills of lading attached as a cash item to the credit of said Cotton Company and obtained credit entries upon the bank passbook of the Cotton Company [Tr. pp. 44-47], and immediately thereafter caused entries to be made in the books of the Cotton Company showing the various amounts credited upon the bank passbook as standing to the credit of the Cotton Company without any offset or charge of any kind, and wilfully failed to make any entry in the books of the Cotton Company disclosing the nature of the transaction, the manner in which said credit account had been obtained, or the existence of the outstanding trust receipts, and thereafter represented to the officers of the Cotton Company that said credits so entered upon the bank passbook and the books of account of the Cotton Company represented funds made and accumulated by him in the conduct of the affairs of the Cotton Company, and upon inquiry made by representatives of plaintiff Bank, represented that the Cotton Company still retained, and that he as secretary of the Cotton Company then had in his custody in the vaults of said Cotton Company all and every the various warehouse receipts sur-

rendered to him by the plaintiff Bank for which it held trust receipts. [Tr. pp. 47, 48.] That said 1091 bales of cotton at the time of their disposition by Sears were of the value of $60,628.72. [Tr. p. 48.] That between said dates Sears, pursuant to the said fraudulent scheme entertained by him and contemporaneous with the fraudulent conversions and misappropriations of the warehouse receipts and the cash represented thereby and the fraudulent representations made to the officers of the Cotton Company and plaintiff Bank, and while acting in his capacity as secretary of said Cotton Company, fraudulently misappropriated or misapplied the moneys wrongfully placed to the credit of the Cotton Company by using said moneys for the purpose of dealing and speculating in cotton, conducting such dealings and speculations at a loss, and paying such losses out of said moneys [Tr. p. 49]; that no part of said $60,628.72 was used in the payment of any of said 87 acceptances held by plaintiff Bank.

That relying upon the false representations of Sears and the deceits practiced upon it by him, said Cotton Company permitted Sears to continue to act as secretary, and to conduct its business and incur indebtedness in its name. That said Cotton Company subsequent to said 19th day of November, 1920, would not have allowed Sears to continue in the position of secretary, nor to conduct any dealings on its behalf or to contract any financial obligations in its name had it known of the frauds and deceits being prac-

ticed upon it and upon plaintiff Bank by Sears. [Tr. pp. 50, 51.]

That because of said frauds and deceits of Sears the Cotton Company has sustained a loss, and has become and is responsible to plaintiff Bank in the amount of $60,628.72. [Tr. p. 51.]

The suicide of Sears on May 3, 1921 [Tr. p. 30], notice of loss to the Bonding Company, as required by the terms of the bond [Tr. p. 29], refusal of the Bonding Company to reimburse the Cotton Company [Tr. p. 30], the entry of judgment May 9, 1922, in the amount of $90,281.00 against the Cotton Company in favor of the plaintiff Bank upon the sight drafts and trust receipts [Tr. p. 30], and the assignment by the Cotton Company to plaintiff Bank of the bond and all rights of action thereunder [Tr. p. 31], are also alleged.

A second cause of action was set forth concerning which no questions are raised under the writ.

Answer.

A demurrer to the complaint as amended having been overruled [Tr. p. 59], the Bonding Company answered, denying directly or for lack of information each of the allegations of the complaint as amended, save those establishing the identity of the parties, the issuance and currency of the bond, the unrestricted powers of Sears as secretary of the Cotton Company, and the entry of judgment against the Cotton Company in favor of the plaintiff Bank. [Tr. pp. 60 to 74.]

Several affirmative defenses were urged:

First, it was alleged that in the application for bond it was represented that there was no cash under the personal control of Sears, only as checks were issued or received for deposit, but that Sears as a matter of fact handled all the cash of the Cotton Company without being required to make an account therefor. [Tr. pp. 74-75.] *Second,* that the Cotton Company in its application for bond represented that all things would be paid by check, but that Sears was permitted to use cash in any manner he pleased. [Tr. pp. 75-76.] *Third,* that the Cotton Company represented in the application for bond that the checks and accounts would be checked up at least once each month by T. J. West, treasurer, but that as a matter of fact no audit was ever made by any person and no verification of the funds on hand was made, and that such audit, if made, would have revealed the loss complained of. [Tr. p. 76.] It was averred that all such representations were warranties and were a part of the bond and were broken in all the respects mentioned. [Tr. pp. 76-77.] *Fourth,* it was alleged that the bond required that the Cotton Company, within ten days after discovery of the dishonesty of Sears, notify the Bonding Company by telegram, and that no such notice was given. [Tr. pp. 78-79.] *Fifth,* it was alleged that the capital stock, save four shares, was owned by T. J. West, who on May 24, 1920, sold and delivered all of his stock to J. B. Sears, who thereafter continued to own the same until his death on May 3, 1921. [Tr. pp. 79-81.] *Sixth,* it was alleged that

the frauds and deceits of Sears complained of were fully known to the Cotton Company and all its officers; that the lien of the defendant-in-error upon the warehouse receipts was surrendered and extinguished; that upon the sale of the cotton represented by the warehouse receipts the bills of lading were returned to the defendant-in-error, who received full payment therefor, and that it sustained no loss by reason of any frauds of Sears. [Tr. p. 82.] *Seventh,* a supplemental answer was filed alleging that under the terms of the bond the employer (Cotton Company) was required to produce its books and records for investigation; that despite repeated demands so to do, said Cotton Company has refused to allow plaintiff-in-error to examine its records. [Tr. pp. 110-114.]

Findings.

The court in special findings of fact [Tr. pp. 118, 155] found the allegations of the amended complaint respecting the first cause of action to be true, and the allegations of the various answers and special defenses of the plaintiff in error to be untrue, *excepting in this important particular:* the court found that on December 1, 1920, Sears purchased 496 of the 500 shares issued and outstanding of the capital stock of said Cotton Company and continued thereafter until his death to be the owner thereof [Tr. pp. 149-151], and that prior to said first day of December, 1920, Sears had wrongfully converted and misapplied cotton of the value of $24,321.97. [Tr. pp. 152-154.]

ARGUMENT.

I. MOTION TO STRIKE BILL OF EXCEPTIONS.

Defendant-in-error served and filed a motion to strike the bill of exceptions on the ground that the same has been signed and certified to this court in contravention of law.

Plaintiff-in-error anticipated this motion (Br. p. 25) and the question raised thereby is the first matter discussed in its brief. (Br. pp. 25-34.) Accordingly, at the outset we devote ourselves to a presentation of the points of fact and law submitted in support of our motion to dismiss and in reply to the argument thereon of the plaintiff-in-error.

Statement of the Facts.

The terms of the United States District Court for the Southern District of California, Southern Division, are held at Los Angeles on the second Monday in January and the second Monday in July of each year (Act of May 16, 1916, Chap. 122, Judicial Code, Sec. 72; Sec. 1057, U. S. Comp. Stats. 1916).

On March 9th, 1925, during the January term of the United States District Court held at Los Angeles, in an action at law tried before the court without a jury, judgment was entered in favor of the defendant-in-error (plaintiff below), and against the plaintiff-in-error (defendant below), in the amount of $30,101.14. [Tr. p. 116.]

On March 14th, 1925, counsel for plaintiff-in-error secured from counsel for defendant-in-error a stipulation, and from the court a special order, extending and enlarging the time within which to prepare and file its bill of exceptions to and including April 15th, 1925. [Tr. p. 514.]

On April 14th, 1925, counsel for plaintiff-in-error secured from counsel for defendant-in-error a second stipulation, and from the court a second special order, extending and enlarging the time within which to prepare and file its bill of exceptions to and including May 15th, 1925. [Tr. p. 515.]

On May 15th, 1925, counsel for plaintiff-in-error secured from counsel for defendant-in-error a third stipulation, and from the court a third special order, extending and enlarging the time within which to prepare and file its bill of exceptions to and including June 15, 1925. [Tr. p. 517.]

On June 8th, 1925, plaintiff-in-error served upon counsel for defendant-in-error its proposed bill of exceptions [Tr. p. 187], and on June 10th, 1925, lodged the same with the clerk of the court. [Tr. p. 513.] This proposed bill consisted of 188 typewritten pages. [Tr. p. 187.]

On June 9th, 1925, by the written stipulation of counsel for the respective parties, the defendant-in-error was allowed to and including July 9, 1925, within which to propose amendments to the proposed bill of exceptions. [Tr. p. 518.]

On July 8, 1925, defendant-in-error served and lodged its proposed amendments. [Tr. p. 485.]

The writ of error herein was allowed, filed and entered on July 6, 1925. [Tr. p. 3.]

On Sunday, July 12, 1925, the term of court at which the judgment was entered expired. (Act May 16, 1916, Chap. 122, Judicial Code, Sec. 72; U. S. Comp. Stats., Sec. 1057.)

On July 22, 1925, counsel for defendant-in-error in writing advised counsel for plaintiff-in-error that the time for settlement of the bill of exceptions had expired. [Tr. p. 488.]

On July 24, 1925, plaintiff-in-error served written notice upon defendant-in-error that it would, on July 28, 1925, present the bill of exceptions for settlement. [Tr. pp. 519, 520.]

The matter of the settlement of the bill of exceptions came on for hearing upon said notice on said 27th day of July, 1925. [Tr. p. 482.]

The defendant-in-error thereupon filed its written objections and objected to the settlement of the proposed bill of exceptions on the ground that the court had lost jurisdiction to settle said bill, specifying the grounds of its objection in detail. [Tr. p. 493.]

In support of the motion to settle the bill the affidavit of Dale H. Parke, one of the attorneys for plaintiff-in-error, was presented and filed [Tr. p. 483], and the counter-affidavit of T. B. Cosgrove, one of the attorneys for defendant-in-error, was presented and filed. [Tr. p. 494.]

The affidavit in support of the motion recites the obtaining of three stipulations of counsel and three special orders of court extending the time to June 15th, 1925, within which to propose the bill, and the filing of the same June 10, 1925; the execution of a stipulation extending the time within which to propose amendments, and the filing of proposed amendments July 8, 1925, the checking of the proposed amendments by counsel for plaintiff-in-error, and his conclusion that they were for the greater part without merit; subsequent telephonic conversations with counsel for defendant-in-error, *no dates being given,* and admission of counsel for defendant-in-error that the proposed amendments were prepared by persons who were perhaps over-cautious, and suggesting that counsel for plaintiff-in-error indicate the proposed amendments he considered meritorious, and those he considered otherwise. The return on July 15, 1925, of plaintiff-in-error's draft of proposed amendments, with notations of counsel for plaintiff-in-error, accompanied by letter dated July 15, 1925, explaining check marks and notations made on copy of proposed amendments and requesting that counsel for defendant-in-error recheck proposed amendments, in view of comments of counsel for plaintiff-in-error respecting same, and indicating willingness of counsel for plaintiff-in-error to again recheck proposed amendments. Subsequent telephonic communications between July 15, 1925, and July 22, 1925, between counsel for respective parties, at which counsel for defendant-in-error stated he was rechecking the amendments and would be finished within a

day or two. The receipt on July 22, 1925, of a letter from counsel for defendant-in-error, returning plaintiff-in-error's copy of proposed amendments, advising counsel for plaintiff-in-error that the time for settling the bill of exceptions had expired, and that the court was without jurisdiction to settle the bill at that time; further stating that if the judge of the trial court took a contrary view of the matter certain suggested amendments would be waived while others would be insisted upon, and expressing a willingness to appear upon written notice at any time before the court to discuss the settlement of the proposed bill. Subsequent conference between counsel for the respective parties on July 23 and 24, rechecking the proposed amendments. That on June 9, 1925, request was made upon counsel for defendant-in-error to indicate what portions of exhibits he desired copied into the record, and statement by counsel for defendant-in-error that he would advise counsel for plaintiff-in-error as to the portions of said exhibits he desired copied into the bill. That counsel for defendant-in-error did not indicate the portions of the exhibits he desired copied into the bill of exceptions until July 25, 1925. The receipt on July 25, 1925, of communication from counsel for defendant-in-error reiterating opinion that time for settlement of bill of exceptions had expired, and that the court was without jurisdiction to settle the same, and suggesting manner of remedying certain defects in the proposed bill in order that question of settlement might be submitted to the court for decision. That sufficient time had not intervened between

July 8th and the end of the term within which to incorporate the proposed amendments. That subsequent to July 22, 1925, affiant had devoted practically his entire time in arriving at an agreement with counsel for defendant-in-error as to proposed amendments. That such agreement was not arrived at until the receipt of said letter of July 25. That the making of the corrections to the bill required a re-writing of a large portion thereof, the employment of a public stenographer on Friday, July 25, and the completion of same on July 27. That defendant-in-error proposed 296 amendments to the bill and later waived 121.

The affidavit of counsel for the defendant-in-error sets forth in chronological order the correspondence passing between counsel for the respective parties respecting the settlement of the bill of exceptions.

1. The first communication is that of July 15, 1925. It is from counsel for plaintiff-in-error to counsel for defendant-in-error. It returns plaintiff-in-error's copy of the proposed amendments and explains the check marks appearing thereon. It suggests a rechecking of the proposed amendments in view of the concessions and rejections of counsel for plaintiff-in-error, and further conferences looking to a settlement of the proposed bill.

2. The letter of July 22, 1925, from counsel for defendant-in-error in response to the letter of July 15, 1925. The opening paragraph of the letter calls attention to the fact that the time for settling the bill of exceptions had expired and that the court was

without jurisdiction to settle the same, but expresses a willingness, in the event the judge of the District Court takes a contrary view, to waive certain suggested amendments, and an intention to insist upon others, and closes with an expression of willingness to confer personally with counsel for defendant-in-error or to appear at any time before the trial judge to discuss the matter of the settlement of the proposed bill.

3. Letter dated July 24, 1925, from counsel for plaintiff-in-error to counsel for defendant-in-error, submitting copy of testimony of witness which had been omitted from the proposed bill of exceptions; also calling attention to service of notice of presentation of bill of exceptions, and further declaring that portions of the minutes and of the by-laws, as well as certain exhibits, are being made for incorporation into bill of exceptions as suggested by defendant-in-error.

4. Letter of July 25, 1925, from counsel for defendant-in-error to counsel for plaintiff-in-error, supplementing communication of July 22, reiterating opinion of counsel for defendant-in-error that the time for settlement of the bill of exceptions had expired and that the court was without jurisdiction to settle the same, and thereafter agreeing that in order that the proposed bill might be presented to the court and the question of settlement passed upon, certain suggestions were made regarding the contents of the proposed bill.

5. Letter of July 27, 1925, from counsel for plaintiff-in-error to counsel for defendant-in-error submitting copy of bill of exceptions as amended and requesting that the same be returned in good time in order that it may be presented to the court on the morning of July 28, 1925, for settlement.

6. The affidavit further recites that no stipulation, oral or written, was entered into between counsel for the respective parties extending the time for the settlement of the bill of exceptions beyond the expiration of the term in which judgment was entered, and that subsequent to the expiration of the term no stipulation was entered into between counsel for the respective parties consenting to the settlement of the bill of exceptions after the expiration of the term; that no order of the court has been made extending the time within which to settle said bill of exceptions beyond the term; that no motion or proceeding in said action was pending and undisposed of upon the termination of the term in which the judgment was entered; and that counsel for plaintiff-in-error had never requested counsel for defendant-in-error to stipulate extending the time to settle the bill of exceptions beyond said term. That the proposed amended bill consists of 257 pages.

The court took the matter under advisement, and thereafter, on July 29, 1925, filed its written order and opinion overruling the objections of the defendant-in-error, settling and allowing the bill of exceptions and allowing the defendant-in-error an exception to the ruling. [Tr. pp. 509, 510, 511.]

On July 30, 1925, the court filed a supplemental order to the order of July 29, 1925, amending the same by striking therefrom certain language inadvertently inserted. [Tr. p. 512.]

Thereafter, on July 31st, 1925 [Tr. p. 513], the bill of exceptions as amended, consisting of 257 pages —typewritten copy [Tr. p. 187]—was filed by the plaintiff-in-error as its engrossed bill of exceptions.

The defendant-in-error now moves to strike the bill of exceptions from the record on the ground that it was signed and certified to this court in contravention of law.

Statement of the Law.

No order of court having been made, nor the consent of the defendant-in-error having been given, *during the term* or thereafter, extending the time within which to settle the bill of exceptions beyond the term in which the judgment was entered, and no motion for new trial or any other motion or proceeding in said action being undisposed of upon the expiration of said term, and no very extraordinary circumstances having been shown justifying the settlement of the bill of exceptions after the expiration of said term, the trial court lost jurisdiction of the matter and was without authority to settle the bill of exceptions.

1. Exporters of Manufacturers' Products v. Butterworth-Judson Co., 258 U. S. 365.

Followed in:

(1) Farm Mortgage & Loan Co. v. Willett, 285 Fed. 42, at 45;

(2) Wick v. U. S., 290 Fed. 191;
(3) Cirino v. American R. Co., 291 Fed. 569, 570;
(4) Merchant v. Dairymen's League, 294 Fed. 281, at 282;
(5) Greyerbiehl v. Hughes Electric Co., 294 Fed. 802, at 807;
(6) Stickel v. U. S., 294 Fed. 808, at 809;
(7) Twohy Bros. v. Kennedy (Ninth Circuit), 295 Fed. 462, at 463;
(8) Goodwin v. U. S., 295 Fed. 856, at 857;
(9) Ritz Carlton etc. Co. v. Gillespie, 1 F. (2d) 921, at 922;
(10) A. T. & S. F. Ry. Co. v. Nichols (Ninth Circuit), 2 F. (2d) 12, at 13.

Earlier decisions of the Supreme Court of the United States are to the same effect.

O'Connell v. U. S., 253 U. S. 142, 146;
Jennings v. Philadelphia, Baltimore & Washington Ry. Co., 218 U. S. 255, 256;
Michigan Insurance Bank v. Eldred, 143 U. S. 293, 298.

Consent of the opposite party should be express and not rest upon implication.

Jennings v. P. B. & W. Ry. Co., 218 U. S. 255, 257-258.

"So grave a matter as the allowance of a bill of exceptions after the close of the term and after the court had lost all judicial power over the record should not rest upon a mere implication from silence. There should be express consent,

or conduct which should equitably estop the opposite party from denying that he had consented."

The consent of the opposite party must be obtained during the term; even written consent after the expiration of the term will not revive the trial court's jurisdiction over the bill of exceptions.

Exporters etc. v. Butterworth-Judson Co., *supra;*

Stickel v. U. S., 294 Fed. 808, 809.

The failure or neglect of plaintiff-in-error to apply to the court during the term at which judgment was entered for an extension of the term was not such a "very extraordinary circumstance" as to justify an exception to the rule.

Farm Mortgage & Loan Co. v. Willett, 285 Fed. 42, 45.

[Note: The Circuit Court of Appeals (Second Circuit) denied a writ of mandamus to compel settlement and filing of the bill of exceptions and the Supreme Court of the United States thereafter refused to issue a writ of certiorari to review the decision of the Circuit Court of Appeals. Farm Mortgage & Loan Co. v. Hazel, 260 U. S. 733.]

Blisse v. U. S. 263 Fed. 961, at 963:

"In United Wrapping Machine Co. v. Stimson, 175 Fed. 1023, 99 C. C. A. 667 (1910), this court dismissed a writ of error; the bill of exceptions not having been signed within the term at which the cause was tried, and the court not having reserved control over the case by rule or order.

"In Glickstein v. United States, 215 Fed. 90, 131 C. C. A. 398 (1914), this court held that, where a defendant convicted of a crime *did not move to have his bill of exceptions signed* until after the expiration of the automatically extended time under rule 5, above referred to, the judge was without power to sign it. And we there said that: 'The extraordinary circumstances mentioned in the Supreme Court cases which justify the signing of the bill after the term has expired relate to circumstances which caused the delay, and cannot be said to include negligence of the party or the importance or difficulty of the question involved.' "

Franklin County v. Furry, 144 Fed. 663, at 664:

"The general rule is that a bill of exceptions must be filed during the term at which judgment is entered or within an extension of time granted during the term. If the party who prepares *and tenders* the bill is not at fault, delay that is occasioned by his adversary or by the act of the judge may be excused. * * * But the fault here was that plaintiff-in-error *failed to present* to the trial judge for allowance and signature of a proper bill of exceptions until long after the expiration of the term and the filing of the record in this court."

Neither is the misunderstanding or lack of knowledge of the rule on the part of counsel such a "very extraordinary circumstance" as to justify an exception to the rule.

Susquehanna Coal Co. v. Casualty Co. of America, 247 Fed. 137.

[Note: The Circuit Court of Appeals (Second Circuit) denied a writ of mandamus to compel settlement and filing of the bill of exceptions.]

Prior to the decision of the Supreme Court of the United States in Exporters etc. v. Butterworth-Judson Co., 258 U. S. 365, there was authority (dicta) to the effect "that such consent may be given even after the term has expired."

Blisse v. U. S., 263 Fed. 961, 966;

Exporters of Manufacturers' Products v. Butterworth-Judson Co. (D. C.), 265 Fed. 907, 908.

[Note: The question before the District Court in the foregoing case was the identical question afterward submitted by the Circuit Court of Appeals (Second Circuit) to the Supreme Court of the United States under the provisions of section 239 U. S. Judicial Code (Comp. Stats., Sec. 1216). Exporters of Manufacturers' Products v. Butterworth-Judson Co., 275 Fed. 1022.]

The duty of drawing up and seasonably tendering a bill of exceptions devolves upon the excepting party.

Michigan Insurance Bank v. Eldred, 143 U. S. 293, at 298-299.

"The duty of seasonably drawing up and tendering a bill of exceptions stating distinctly the rulings complained of and the exceptions taken to them, belongs to the excepting party, and not to the court. * * * Any fault or omission in framing or tendering a bill of exceptions being the act of the party and not of the court, cannot

be amended at a subsequent term, as a misprison of the clerk in recording inaccurately or omitting to record an order of the court might be."

Disregard of the established rules of procedure through inadvertence of counsel, resulting in a defective bill, imposes upon the appellate tribunal the duty of following the mandatory provision of the statute and dismissing the bill.

Blisse v. U. S., 263 Fed. 961, at 961-962.

"We are not insensible to the fact that the dismissal of a cause without passing on the merits, because the inadvertence of counsel has disregarded an established rule or procedure, is to impose upon the litigant an extreme penalty. At the same time we are compelled to adhere to established rules of orderly procedure, which experience has shown to be important in the administration of justice. The rules respecting the preparation of a case to be brought to an appellate court on writ of error are not uncertain, and are not obscure, and it is to be assumed that they are familiar to counsel. A failure to observe them, as has frequently been remarked, only tends to confusion, and to the demoralization of the procedure of the court. E. I. Du Pont de Nemours & Co. v. Smith, 249 Fed. 409, 161 C. C. A. 377. To disregard such rules is to introduce uncertainty and perplexity into the administration of justice, and as Mr. Justice Story remarked is destructive of the law as a science. Story's Eq. Pl., Sec. 544."

Oxford & Coast Line R. Co. v. Union Bank, 153 Fed. 723, at 728.

"While it is not the policy of the court to dismiss writs of error and cases of appeal on account of slight technicalities, at the same time the rules of this court, as well as the rules of the Circuit Court, are plain and easily understood. In this instance the provision of the statute relating to the question at issue is mandatory and must be enforced. It is incumbent upon attorneys who practice in the Federal Courts to observe and strictly follow the rules of practice and procedure in preparing and presenting bills of exceptions * * *. It is essential to the orderly procedure of the courts that attorneys should comply with the rules relating to the same, otherwise it would be useless to promulgate rules for the guidance of those who may seek to review the action of the lower court.

"Mr. Justice Story in his work on Equity Pleading (section 544), in commenting upon the necessity of adhering strictly to the prescribed forms of procedure, says: 'The want of due form constitutes a just objection to the proceedings in every court of justice, for to reject all form would be destructive of the law as a science and would introduce great uncertainty and perplexity in the administration of justice. Every irregularity of this sort is fraught with inconvenience and generally tends to delays and doubts, and it has been well remarked that infinite mischief has been produced by the facility of courts of justice in overlooking errors of form. It encourages carelessness and places ignorance too much on a footing with knowledge among those who practice the drawing of pleadings.' "

Mound Coal Co. v. Jeffrey Mfg. Co., 233 Fed. 913, at 919.

Discussion.

Whatever doubt may have existed prior to the decision of the Supreme Court of the United States in the case of Exporters of Manufacturers' Products v. Butterworth-Judson Co., 258 U. S. 365, as to the effect of proceedings had and taken subsequent to the expiration of the term, is dispelled by the language of the opinion in that case.

Not even express written stipulation of the parties executed subsequent to the term at which judgment was entered will legalize the settlement of the bill. In the present case not only is there no written stipulation consenting to the settlement of the bill subsequent to the term, but on the contrary the written communications affirmatively disclose a lack of consent.

During the term plaintiff-in-error obtained three special orders of the court and stipulations of counsel extending the time within which to propose the bill. None of these extended the time beyond the expiration of the term. Neither was any request made for a stipulation extending the time beyond the term. The remaining question presented upon this motion is: Do the facts occurring prior to the expiration of the term come within the meaning of the term "very extraordinary circumstances justifying the settlement of the bill after the expiration of the term"?

In order that it may have a correct understanding of the facts that occurred before and those that occurred subsequent to the expiration of the term, we invite the court's attention particularly to that por-

tion of the affidavit in support of the motion to settle the bill of exceptions appearing in the transcript at pages 485 to 488. This affidavit is not inartificially nor carelessly drawn; it is artfully and studiously prepared. We call attention to the fact that no attempt is made to set forth the dates of any occurences transpiring between July 8 and July 15, although this is the important and controlling period—the term ending on Sunday, July 12th. The letter of July 15th, written by counsel for plaintiff-in-error, is the tie-point from which there is no escape. The affidavit declares that prior to the preparation of the letter of July 15th affiant had spoken with one of the attorneys for the defendant-in-error over the 'phone respecting the proposed amendments. No mention is made, however, of the date of this telephonic conversation. The nature of the conversation, however, as disclosed by the affidavit read in conjunction with the language of the letter of July 15th, would indicate that the telephonic conversation occurred immediately preceding the dictation of the letter. This appears particularly probable in view of the fact that the affidavit declares that affiant *had checked over* the proposed amendments and *found them to be without merit before he telephoned* to the attorney for the defendant-in-error, at which time he made known his views respecting the proposed amendments, whereupon counsel for the defendant-in-error suggested that the proposed amendments be check-marked to correspond with affiant's opinion of their merit or lack thereof. Compli-

ance with this suggestion was the letter of July 15, 1925.

The only circumstances occurring prior to the expiration of the term (Sunday, July 12, 1925) which in our opinion may be considered is the fact that between the time of the service of the proposed amendments and the expiration of the term, a period of three court days (four calendar days) intervened. At that time, as we view it, either one of two things occurred. Counsel for plaintiff-in-error either misunderstood the rule requiring the settlement of the bill during the term or some extension thereof obtained during the term, or understanding the rule they are guilty of negligence in failing to secure an order or stipulation extending the term. An abundance of time remained within which to secure a stipulation and special order of court of the character of any of the three theretofore given and made. Neither a misunderstanding of the rule, nor a neglect to obtain an extension of the term constituted "very extraordinary circumstances" justifying an exception to the rule.

We wish to emphasize what heretofore has been mentioned only casually, namely, that the proposed bill of exceptions served June 8th, 1925, and lodged with the clerk June 10th, 1925, consisting of 188 pages —typewritten copy [Tr. p. 187], was not the bill of exceptions served July 27, 1925, and settled by the court and filed with the clerk on July 31, 1925. The bill settled consisted of 257 pages—typewritten copy. [Tr. p. 187.] The difference in the original bill as proposed and the amended bill as settled was due to

an incorporation therein or addition thereto of 175 amendments proposed by defendant-in-error.

The plaintiff-in-error relies, among others, upon two decisions of the Circuit Court of Appeals for the Ninth Circuit. They are:

1. Sutherland v. Pearce, 186 Fed. 783;
2. Pacific Bank v. Hannah, 90 Fed. 72.

Concerning Sutherland v. Pearce, we direct the court's attention to the language of the opinion appearing on pages 786 and 787 of volume 186, Fed Rep., being subdivision 3. It discloses that on June 1, 1910, the court entered an order that the defendants should have four months within which to prepare and file for allowance their bill of exceptions. That *within this time* the bill of exceptions was filed and signed by the court, viz., on September 15, 1910.

Concerning Pacific Bank v. Hannah, 90 Fed. 72, we direct the court's attention to syllabus number one, reading:

> "1. Bill of Exceptions.—Time for Allowance. The filing of a bill of exceptions during the term of court at which judgment is rendered is sufficient to preserve the rights of a party, and to authorize its allowance and settlement after the term."

The language of the opinion (90 Fed. 76) appears to bear out the statement appearing in the syllabus. It will be observed that no mention is made respecting an order of court or stipulation of counsel extending the time for settlement of the bill beyond the term. *As a matter of fact, there was such a stipu-*

lation in the record, concerning which more is said hereafter. Briefly referring to the authorities cited in support of the statement of the court, we have—

(a) *Woods v. Lindvall,* 48 Fed. 73.

In this case, at the term in which judgment was rendered, a *motion for new trial* was made. The motion for new trial *was not passed upon* until a subsequent term. The court in this manner retained jurisdiction of the action. At the term in which the motion for new trial was denied the bill of exceptions was settled. Passing upon this point, the court says:

> "It is true that in several cases cited by counsel for defendant-in-error (citing Supreme Court decisions) it was held in effect that in the absence of an order of court extending the time a bill of exceptions covering errors committed at the trial cannot be allowed and filed (unless by consent of parties) after the term has expired at which the judgment was rendered. But in none of these cases did the question arise whether a bill of exceptions may not be allowed and filed at the term when the motion for a new trial is finally acted on, even though such action is taken at a term subsequent to the entry of judgment; *and that is the precise question which confronts us in the case at bar.*"

(b) *Waldron v. Waldron,* 156 U. S. 361.

The first syllabus reads:

> "A bill of exceptions may be signed after the expiration of the term at which the judgment was rendered, *if* done by agreement of parties *made during that term.*"

The decision is by Mr. Justice White. At page 378 of the 156 U. S. Rep., the opening paragraph of the opinion reads:

> "The signing of the bill of exceptions after the expiration of the term at which the judgment was rendered, was lawful if done by consent of parties given *during that term.*"

Citing, among others:

> *Davis v. Patrick,* 122 U. S. 138,

which was also cited in the Pacific Bank case.

(c) *U. S. v. Gotlieb Breitling,* 20 How. 252.

This decision is cited (Br. p. 29) by counsel for plaintiff-in-error.

This case, decided in 1857, holds that the general rule of a Circuit Court of the United States in Alabama, adopting the practice of the state courts in the matter of the settlement of bills of exceptions, is not binding upon the judges of said court. The decision also holds that the time within which to settle bills of exceptions must depend upon the rules and practice of the court and *on its own judicial discretion.* It is then declared:

> "In the case before us, the judge who tried the case has deemed it his duty to seal and certify the exception to this court; and under the circumstances stated in the exception and the note, we think he was right in doing so, and that this exception is legally before this court as a part of the record of the proceedings of the court below."

What was stated "in the exception and the note" the record does not disclose. Were the matters referred to in the "note" recited in the opinion of the court the correctness of the ruling might be at once manifest.

(d) Counsel for the defendant also refers to—

Hume v. Bowie, 148 U. S. 248.

At page 253 of the decision (148 U. S. Rep.) the court declares:

> "The rule is unquestionably correctly laid down in Muller v. Ehlers, 91 U. S. 249, that when judgment has been rendered and the term expires, a bill of exceptions cannot be allowed, signed and filed as of the date of the trial, in the absence of any special circumstances in the case, and without the consent of the parties or any previous order of court. But it is always allowable, if the exceptions be seasonably taken and reserved, that they may be drawn out and signed by the judge afterwards, and the time within which this may be done must depend upon the rules and practice of the court and the judicial discretion of the presiding judge. Dredge v. Forsyth, 2 Black 563, and Chateaugay Iron Company, Petitioner, 128 U. S. 544. * * *
>
> "The rules also provided that the terms of court might be prolonged by adjournment for the purpose of settling bills of exceptions, *and an order was accordingly entered prolonging the term at which this judgment was rendered for the purpose of doing that in this case.* This was equivalent to the practice in many jurisdictions of entering an order granting additional time, after the

expiration of the term, in which to settle such bills."

(e) *Dredge v. Forsyth,* 2 Black, U. S. 562.

This case was decided in 1862. Contention was made in this case that the exceptions must be drawn out and sealed by the judge *before the jury retires from the bar of the court.* The court held otherwise and declared (2 Black, U. S. 568):

> "Great inconvenience would result from such a requirement, and in point of fact there is no such rule. On the contrary, it is always allowable, if the exception be seasonably taken and reserved, that it may be drawn out in form and sealed by the judge afterward, and the time within which it may be so drawn out and presented to the court must depend on the rules and the practice of the court and the judicial discretion of the presiding justice. Such was the rule laid down by this court in U. S. v. Brietling (20 How. 254), and we see no reason to qualify it on the present occasion."

By the statement, "the time within which" the bill of exceptions may be presented to the court "must depend on the rules and practice of the court and the judicial discretion of the presiding justice," is meant precisely what is stated, namely, that the presiding justice may, in his discretion, allow such time as he sees fit to settle the bill of exceptions. If the term expires, however, without any such order of the court having been made, then, according to the authorities (Exporters' etc. v. Butterworth-Judson Co., *supra,* it

is too late after the term has expired to obtain such order.

(f) *Chateaugay Ore & Iron Company, Petitioner,* 128 U. S. 544.

This case is cited and is relied upon by plaintiff-in-error (Br. p. 30). At page 556 of the opinion (128 U. S.), the court, in declaring that upon the facts of the case then under consideration the decision in a leading case, namely, Muller v. Ehlers, 91 U. S. 249, had no application, uses this language:

> "That decision has no application to the present case because the rights of the defendant were saved by the express order of the court, made *during the term,* and by a sufficient compliance on the part of the defendant with the rules of the Circuit Court, and by what must be held to have been the consent of the plaintiff."

Accordingly, it appears that there was an express order of the court made during the term extending the time within which to settle the bill of exceptions. That, in the next place, there was a compliance with the rules of the court, and in the third place the facts indicated that the plaintiff consented to the extension. In the present case there is no order, express or implied, of the court made during the term extending the time to settle the bill of exceptions beyond the term. There is no consent on our part to such an extension, but on the contrary an objection was raised by defendant-in-error at the first opportunity following the expiration of the term, and persisted in thereafter.

This analysis of the authorities cited by Circuit Judge Morrow in the Pacific Bank v. Hannah case (90 Fed 72) discloses that in *each* of the authorities relied upon—save perhaps the possible exceptions of the case of U. S. v. Breitling, 20 How. 252, where special circumstances not set forth in the opinion appear to have controlled the decision of the court—there was either an order of court or a stipulation of the parties, made during the term, extending the period within which the bill of exceptions might be settled to a time beyond the expiration of the term in which the judgment was rendered. We stated heretofore that in the Pacific Bank case there was such a stipulation. This fact does not appear from a reading of the opinion, however. Nevertheless, it is a fact that the court had before it such stipulation. At the time of the decision, on the Circuit Court of Appeals for the Ninth Circuit were Circuit Judges Morrow, Ross and Gilbert. This Pacific Bank case again came before the Circuit Court of Appeals for the Ninth Circuit in October, 1924. At that time sitting upon said court were Circuit Judges Gilbert, Ross and Hunt. The matter came up upon a writ of error to the District Court of the United States for the Southern District of California, Southern Division, in the case entitled:

A. T. & S. F. Ry. Co. v. Nichols, 2 F. (2d) 12.

The following are extracts from the opinion of the court:

Counsel for defendant-in-error move to strike out the bill of exceptions upon the ground that it was not settled during the term in which the case was tried and that no extension was granted.

"Plaintiff-in-error cites the opinion of this court in Pacific Bank v. Hannah, 90 Fed. 72, 32 C. C. A. 522, where it was said that the bill of exceptions, having been filed within the term at which judgment was rendered, was sufficient to preserve the rights of a party presenting the bill of exceptions for allowance and settlement.

"That case is not in point, for there the findings and conclusions were filed March 24, 1897, and judgment was rendered on that day. Orders extending time to file exceptions to the findings and conclusions were made on that day and several times thereafter *during the term of court.* The bill of exceptions was filed March 28, and on June 2d a proposed amendment was filed and stipulation was had between counsel, extending time for further amendments until matters could be brought to the attention of the court. The February term was adjourned June 30, 1897, but the bill of exceptions was not signed until July, and doubtless upon the authority of Waldron v. Waldron, 156 U. S. 361, cited in the opinion. The signing of the bill of exceptions after the adjournment of the term at which judgment was rendered was sustained."

We believe that the bill of exceptions was settled, signed and certified to this court in contravention of law, in that the term had expired before the same was offered for settlement, and accordingly that the motion to strike the same should be granted.

If our contention is correct that the bill of exceptions has been signed and certified to this court in contravention of law, and the motion to strike is granted, thirty of the thirty-one assignments of error will be disposed of. The first assignment of error, viz., that the amended complaint does not state a cause of action [Tr. p. 522], is the only one that may be considered without an examination of the evidence.

In the absence of a bill of exceptions, questions respecting the admissibility of evidence are excluded from consideration, and the review is confined to what appears upon the face of the pleadings and the findings.

Porto Rico v. Emmanuel, 235 U. S. 251-255;
Rosaly v. Graham, 227 U. S. 584, 590;
Buessel v. U. S., 258 Fed. 811, 818.

II. ASSIGNMENTS OF ERROR.

Although There Are Thirty-one Assignments of Error (Brief, Pages 34-48) Relied Upon by the Plaintiff in Error in Its Brief, Only Two Questions Are Reviewable Under the Writ. They Are:

1. *Does the amended complaint state facts sufficient to constitute a cause of action against the defendant?* and

2. *Do the facts found support the judgment?*

The first question stated being assignment of error number 1 [Tr. p. 522], raises a question of law presented to the court upon which an adverse ruling was

made and an exception was then taken. The second question stated may be raised under the writ because of the fact that the court made special findings of fact. [Tr. pp. 118 to 155.] No other question is raised by the writ for the reason that all assignments, save the second (motion for nonsuit [Tr. p. 379]), in which instance the plaintiff-in-error failed to preserve an exception to the ruling of the court, deal with the sufficiency of the evidence to support the judgment, and although the plaintiff-in-error moved the trial court to make special findings in its favor, the court was not requested to rule and did not pass upon the motion or request; neither is there any exception noted upon which an assignment of error might be predicated.

The Facts Involved.

This action was tried and determined by a court without the intervention of a jury, the attorneys of record having filed with the clerk a stipulation in writing waiving a jury. [Tr. p. 116.]

The court made special findings of fact in favor of the defendant-in-error. [Tr. pp. 118-154.]

There is printed in the transcript of record [Tr. pp. 467-477] a request of plaintiff in error for special findings of fact. These special findings had been presented at a former trial of the case and by stipulation of counsel and consent of the court [Tr. p. 462] it was agreed that said special findings might be considered as refiled and the request again made. There is nothing in the record to disclose that the findings were

ever presented to or considered by the trial court. There is no ruling of the trial court upon such "Request for Special Findings of Fact"; there is no request for a ruling, and there is no exception noted to any ruling of the court upon the special findings or to the failure of the court to rule upon such request for special findings. It is apparent that counsel for plaintiff in error attached no significance to the refiling of the special findings of fact—the stipulation covering the matter having been suggested and presented by counsel for defendant in error [Tr. p. 462]—for immediately following such stipulation counsel presented orally a motion [Tr. pp. 462-466], which in effect is a request for declarations of law and special findings of fact. Upon its presentation a colloquy ensued between the trial court and counsel presenting the motion [Tr. p. 466] which discloses that the court made no ruling upon the motion or request; that counsel for plaintiff in error not only did not request a ruling upon the motion but expressed his understanding that no ruling was being made and apparently that he was satisfied with this action on the part of the court, and there is not elsewhere in the record any ruling upon this motion, any request for a ruling, or any exception preserved upon which an assignment of error might be predicated.

The plaintiff in error has assigned 31 specifications of error [Tr. pp. 522-536]. The first assignment of error specifies the overruling of a demurrer to the amended complaint [Tr. p. 522]; the record discloses an exception to the ruling [Tr. p. 59]. The second

assignment specifies the overruling of the motion for nonsuit [Tr. p. 523], the record discloses no exception to the ruling [Tr. p. 379]. Assignments numbered 3 to 26, both inclusive, assign the insufficiency or lack of evidence to support the findings of the court [Tr. pp. 523-535]. Assignments numbered 27 and 28 specify that the court erred in awarding judgment for the defendant in error and that said judgment is contrary to law and the cause made and facts stated in the pleadings and record [Tr. p. 535]. Assignment numbered 29 specifies the failure of the court to grant the request of plaintiff in error for special findings of fact [Tr. p. 535]. There was no ruling of the trial court and no exception taken [Tr. pp. 466-467. Assignments numbered 30 and 31 specify the failure of the court to find on two particular matters therein mentioned [Tr. pp. 535, 536]. There is no exception noted in the record to support this assignment [Tr. pp. 466, 467].

There is nowhere in the brief any reference to the pages of the transcript of record showing the manner in which the error assigned arose, the ruling of the court, or the preserving of an exception; neither is there in the printed transcript of record appropriate notations *i. e.*, exception number 1, exception number 2, etc.), indicating that the matter there occurring constitutes the subject matter of an exception.

THE LAW INVOLVED.

Nature and Extent of Assignments Reviewable.

Where an action is tried by the court without a jury the rulings of the court in the progress of the trial if excepted to at the time and duly presented by a bill of exceptions may be reviewed upon writ of error; when the finding is special such review may extend to the determination of the sufficiency of the facts found to support the judgment; if it is sought to test the sufficiency of the evidence to support the judgment special requests to the trial court to find the facts must be made and if the request is denied and an exception taken the denial presents a question of law.

(1) Revised Statute, Section 649.

> "Issues of fact in civil cases in any Circuit Court may be tried and determined by the court, without the intervention of a jury, whenever the parties, or their attorneys of record, file with the clerk a stipulation in writing waiving a jury. The finding of the court upon the facts which may be either general or special shall have the same effect as the verdict of a jury." Comp. St. 1918, Sec. 1587.

(2) Revised Statute, Section 700.

> "When an issue of fact in any civil cause in a Circuit Court is tried and determined by the court without the intervention of a jury, according to section 649, the rulings of the court in the progress of the trial of the cause, if excepted to at the time, and duly presented by a bill of exceptions, may be reviewed by the Supreme Court upon a

writ of error or upon appeal; and when the finding is special, the review may extend to the determination of the sufficiency of the facts found to support the judgment." Comp. St. 1918, Sec. 1668.

(3) U. S. v. Columbia and N. R. R. Co., 274 Fed. 625 (C. C. A., 9th Cir.);

(4) Stoffregan v. Moore, 271 Fed. 680, 681.

"The fundamental rule that on writ of error only questions of law may be reviewed may serve as a guide to counsel on the trial of actions at law without a jury The court at its discretion may make findings of fact either general or special. If they are special the question of law as to whether the special findings support the judgment may be reviewed; also the objections to the omission or exclusion of evidence during the trial. If it is sought to test the sufficiency of the evidence to support the judgment some request to the trial court to find facts or declare the law must be made, and if the requests are denied, then the denial presents a question of law. * * * There is a bill of exceptions which purports to contain the evidence taken at the trial but such bill of exceptions is not an agreed statement of the case *and it contains no ruling of the trial court upon which the assignments of error can be based.*"

(5) Mason v. U. S. 219 Fed. 547, 549.

Excessive Number of Assignments Condemned.

The Supreme Court and the Circuit Courts of Appeals have repeatedly condemned the practice of filing a large number of assignments. It perverts the pur-

pose sought to be subserved by the rule requiring assignments. It points to nothing and thwarts the purpose of the rule by which it was intended to present to the court a clear and concise statement of material points on which plaintiff in error intends to rely.

(1) Ches. & Del. Canal Co., v. U. S. 250 U. S. 123, 124.

"There are forty-one assignments of error in this court which counsel in their brief compress into five questions and these resolve themselves at once into three * * *. Such a record constrains us to repeat the following:

'This practice of unlimited assignments is a perversion of the rule, defeating all its purposes, bewildering the counsel of the other side, and leaving the court to gather from a brief, often as prolix as the assignments of error, which of the latter are really relied on.' "

(2) Central Vermont Ry. Co. v. White, 238 U. S. 507, 509;

(3) Phillips etc. Construction Co. v. Seymour, 91 U. S. 646, 648.

"The object of the rule requiring an assignment of errors is to enable the court and opposing counsel to see on what points the plaintiff's counsel intend to ask a reversal of the judgment, and to limit the discussion to those points. This practice of unlimited assignments is a perversion of the rule, defeating all its purposes, bewildering the counsel of the other side, and leaving the court to gather from a brief, often as prolix as the assignments of error, which of the latter are

really relied on. We can only try to respond to such points made by counsel as seem to be material to the judgment which we must render."

(4) Fitter v. U. S. 258, Fed. 567, 569;

(5) Clark v. U. S. 258 Fed. 437 at 438.

Necessity for Obtaining a Ruling and Noting an Exception.

Whether there is any substantial evidence to sustain a finding is reveiwable as a question of law only when a request or motion is (1) *made,* (2) *denied,* and (3) *excepted to,* or some other like action is taken which *fairly presents* that question to the trial court *and secures its ruling thereon* during the trial

(1) Wear v. Imperial Window Glass Co., 224 Fed. 60, 63;

(2) Mercantile Trust Company v. Wood, 60 Fed. 346, 348.

"The special finding referred to in this conclusion is not a report of the evidence, but it must be, like the special verdict of a jury, a finding of the ultimate facts which the evidence establishes. The only question the special finding presens that would not be presented by a general finding is whether or not, in any view, the facts found in it are sufficient to support the judgment. With the single exception of this question, which is presented by the special finding itself, there are only two methods by which questions of law can be so presented to the court that tries the facts that this court can review them by writ or error. These methods are, first, by seasonable objections

and exceptions to the rulings of the court upon the admission or rejection of evidence, and, second, by requesting the court before the trial is ended, to make declarations of law, and *excepting to its refusal* to do so, and to its declarations of law, *if any,* that *do not accord with the propositions asked,* in exactly the same way as instructions to a jury would be requested, and the rulings of the court giving or refusing them would be excepted to, if the trial was before a jury. The finding of the court, whether general or special, performs the office of a verdict of a jury. When it is made and filed, the trial is ended. Exceptions to the finding, or to statements of legal conclusions contained in it, or in an opinion in which it is contained, or in an opinion filed with it, avail nothing. They are as futile as exceptions to the verdict of a jury. When a case comes to this court upon a writ of error, this is a court for the correction of the errors of the court below solely. To enable us to review those errors in a case tried by the court it must appear that the legal propositions on which they rest were presented to that court *and ruled upon* before the trial ended, unless they are involved in the single question whether or not the facts found in a special finding are sufficient to support the judgment. It is, in the words of the statute, 'the rulings of the court in the progress of the trial of the case,' and these only, that we are authorized to review, unless such rulings are involved in the single question we have mentioned. (Citing cases)."

(3) Seep v. Ferris-Haggarty etc. Co., 201 Fed. 893, 895;

(4) Pennsylvania Casualty Co. v. White Way (C. C. A. 9th Cir.), 210 F. 782, 784.

"When an acion at law is tried before a jury, their verdict is not subject to review unless there is absence of substantial evidence to sustain it, and even then it is not reviewable unless a request has been made for a peremptory instruction and *an exception taken* to the ruling of the court. When a jury is waived, and the case is tried by the court, the general finding of the court for one or the other of the parties stands as the verdict of the jury, and may not be reviewed in an appellate court unless a lack of evidence to sustain the finding has been suggested by a request for a ruling thereon, or a motion for judgment, or some motion to present to the court the issue of law so involved, before the close of the trial. (Citing cases.)"

Exceptions of No Avail Unless Taken at the Trial.

An exception must show that it was taken and preserved at the trial and this must appear affirmatively on the record. No bill of exceptions can be entertained by the Appellate Court unless it appears from the record that an exception was taken to the ruling of the court below.

(1) U. S. v. Carey, 110 U. S. 51, 52;

(2) Mound Coal Co. v. Jeffrey Mfg. Co., 233 Fed. 913, 918.

Assignments Must Be Specific.

General assignments of error will not be entertained.

(1) "Rule XI. Assignment of errors. The plaintiff in error or appellant shall file with the clerk of the court below, with his petition for the writ of error or appeal, any assignment of errors, which shall set out separately and particularly each error asserted and intended to be urged."

(2) Guerini Stone Co. v. Carlin Construction Co., 248 U. S. 334, 348;

(3) U. S. v. U. S. F. & G. Co., 236 U. S. 512, 529;

(4) McDermott v. Severe, 202 U. S. 600, 610;

(5) Bank of Italy v. Roneo & Co. (C. C. A. 9th Cir.), 287 Fed. 5, 8;

(6) Grape Creek Coal Co. v. Farmers' Loan & Trust Co., 63 Fed. 891, 894.

"The second and third specifications of error do not, in conformity with the eleventh rule of this court, 'set out separately and particularly' the error intended to be urged. An assignment cannot be good, under this rule, if it is necessary to look beyond its terms, to the brief, for a specific statement of the question sought to be presented."

(7) The "Francis Wright", 105 U. S. 381, 389.

"There is another equally fatal objection to this bill of exceptions. An evident effort has been made here, as it has been before, to so frame the exceptions as, if possible, to secure a re-examination of the facts in this court. The transcript which has been sent up contains the pleadings and all the testimony used on the trial below. The bill of exceptions sets forth that at the trial the pleadings were read by the respective parties, and the testimony then put in on both

sides. This being done, the libellants presented to the court certain requests for findings of fact and of law. These requests were numbered consecutively, sixteen relating to facts and three to the law. Afterwards, six additional requests for findings of fact were presented. It is then stated that the court made its findings of fact and of law and filed them with the clerk, together with an opinion in writing of the circuit justice who heard the cause. The libellants then filed what are termed exceptions to the findings and the refusals to find. In this way exceptions were taken separately to each and every one of the facts found and the conclusions of law, and to the refusal to find in accordance with each and every one of the requests made. The grounds of the exceptions are not stated. Many of the requests of the libellants are covered explicity by the findings as actually made, some being granted and others refused.

"We have no hesitation in saying that this is not a proper way of preparing a bill of exceptions to present to this court for review rulings of the Circuit Court such as are now complained of. A bill of exceptions must be 'prepared as in actions at law', where it is used, 'not to draw the whole matter into examination again', but only separate and distinct points, and those of law."

(8) Wear v. Imperial Window Glass Co., 224 Fed. 60, 63.

"The only question the specifications of error attempt to present is whether or not the evidence, which is conflicting, sustains the finding and judgment of the court. They invite this court, in other words, to retry this case and to determine whether or not under the applicable law the

weight of the evidence sustains the finding and judgment. But the case was tried by the court below without a jury, and its decision of that issue is not reviewable in this court. It is, like the verdict of a jury, assailable only on the ground that there was no substantial evidence in support of it, and then it is reviewable only when a request has been made to the trial court before the close of the trial that it adjudge, on the specific ground that there was no substantial evidence to sustain any other conclusion, either all the issues or some specific issue in favor of the requesting party. No such request was made in this case, and the specifications of error, therefore, present no question reviewable by this court. When an action at law is tried without a jury by a federal court, and it makes a general finding, or a special finding of facts, the act of Congress forbids a reversal by the appellate court of that finding, or the judgment thereon, 'for any error of fact' (Revised Statutes, Sec. 1011 [U. S. Comp. Stat. 1913, Sec. 1672, p. 700]), and a finding of fact contrary to the weight of the evidence is an error of fact.

"The question of law whether or not there was any substantial evidence to sustain any such finding is reviewable, as in a trial by jury, only when a request or a motion is made, denied, and *excepted to,* or some other like action is taken which fairly presents that question to the trial court and *secures its ruling thereon* during the trial. (Citing cases)."

The Object and Purpose of an Exception.

The sole purpose of a bill of exception and assignment of errors is to bring the matters complained of

separately and clearly (1) before the trial judge so that he may have the opportunity to grant relief if he thinks proper, (2) before counsel for defendant in error, so that he may be advised of the precise points to be made in argument, and (3) before the appellate court, so that it may readily perceive the points to be decided and the portions of the record on which they depend.

(1) Fillippon v. Albion Vein Sale Co., 250 U. S. 76, 82.

"* * * the primary and essential function of an exception is to direct the mind of the trial judge to the point in which it is supposed that he has erred in law, so that he may reconsider it and change his ruling if convinced of error, and that injustice and mis-trials due to inadvertent errors may be obviated."

(2) Guerini Stone Co. v. Carlin Construction Co., 248 U. S. 334 at 338;

(3) U. S. v. U. S. F. & G. Co., 236 U. S. 512 at 529.

"An exception therefore furnishes no basis for reversal upon any ground other than the one specifically called to the attention of the trial court."

(4) Robinson & Co. v. Belt, 187 U. S. 41, 50.

"While it is the duty of this court to review the action of subordinate courts, justice to those courts requires that their alleged errors should be called directly to their attention, and that their action should not be reversed upon questions which the astuteness of counsel in this court has evolved from the record."

(5) Buessel v. U. S. 258 Fed. 811, 819.

> "In Michigan Insurance Bank v. Eldred, 143 U. S. 293, 298 * * *, Mr. Justice Gray stated the rule and declared that by the uniform course of decision no exceptions to ruling could be considered, unless they were taken at the trial and were also embodied in a formal bill of exceptions * * *. The court held, therefore, that an exception furnishes no basis for reversal upon any ground other than the one *specifically* called to the attention of the trial court."

Bearing in mind the principles announced and the practices prescribed by the authorities just cited, we draw the following conclusions respecting plaintiff in error's thirty-one assignments of error.

1. Assignment number 1 [Tr. p. 522]—overruling demurrer to the amended complaint—may be reviewed, being an adverse ruling upon a question of law, an exception having been preserved. [Tr. p. 59.]

2. Assignment number 2 [Tr. p. 523]—denying motion for non-suit—may not be reviewed, no exception having been taken at the time to the ruling of the court. [Tr. p. 379.]

3. Assignments numbered 3 to 31, both inclusive, may not, neither may any of them be reviewed because of the failure of the plaintiff in error during the trial to present a request or motion submitting the matters therein specified for the court's consideration, obtaining a ruling thereon and preserving an exception to such ruling.

4. Assignments numbered 3 to 26, inclusive [Tr. 523-535], specify the alleged insufficiency of the evi-

dence to sustain the findings. Of these twenty-four assignments the following, towit: numbers 3, 5, 8, 9, 10, 11, 12, 15, 16, 17, 18, 19, 21, 22, 23, 24, 25 and 26, may not be considered for the reason that they do not conform with Rule 11 of this court. They are not specific and in order to obtain a specific statement of the question sought to be presented, it is necessary to look beyond the terms of the assignment to the brief of the plaintiff in error.

5. Assignments numbered 27 and 28, assigning generally as error the finding for the defendant in error and against the plaintiff in error, and assignments numbered 30 and 31, specifying the failure of the court to find in certain particulars therein specified are subject to the same criticism as those assignments specified in the immediately preceding paragraph number 3, namely, they do not comply with Rule 11 of the court; they are not specific and it is necessary to examine the brief of the plaintiff in error to obtain a specific statement of the question sought to be presented.

6. Assignment number 29 specifying the refusal of the court to make findings in accordance with "request for special findings of fact" of plaintiff in error may not be assigned for the reason that the special findings were not actually and fairly presented to the court for ruling; were not passed upon by the court, and no exception to the ruling or failure of the court to rule was preserved.

The failure of the plaintiff in error to obtain a ruling upon its oral motion for declarations of law and special findings [Tr. p. 466] or to call to the attention of the court and obtain a ruling upon its written special findings with the accompanying absence of any exceptions taken and preserved during the course of the trial, limits the review of this court under the writ to the questions:

1. *Does the Amended Complaint State Facts Sufficient to Constitute a Cause of Action Against the Defendant?* and
2. *Do the Facts Found Support the Judgment?*

III. SEVEN POINTS OF PLAINTIFF IN ERROR.

Plaintiff in error, as we believe, in disregard of the rules and practice of this court, as outlined in the preceding subdivision of this argument, after having filed an omnibus assignment of errors consisting of 31 separate specifications, arranges the assignments into seven groups setting forth for each group his deduction of the point raised by the various assignments in that particular group. These seven contentions have been by counsel for plaintiff in error arranged under seven general headings (Br. pp. 49-52) and thereafter in consecutive order have been presented for the court's consideration (Br. pp. 53-139). We shall undertake a consideration of these seven "Points of Plaintiff in Error" in the order of their announcement.

Points of Plaintiff in Error Numbers I and II Answered.

The assignments of error numbers 1, 2, 3, 15, 22, 27, 28 and 29 are by plaintiff in error grouped under two headings, namely:

(I) "The Cotton Company sustained no loss by reason of the alleged acts of J. B. Sears, its secretary, in wrongfully converting or wilfully misapplying the 1091 warehouse tickets or the cotton represented thereby, and which were covered by unredeemed trust receipts held by plaintiff bank, and the court erred in finding that any such loss was incurred by the Cotton Company;" and

(II) "The first cause of action in plaintiff's complaint as amended does not state facts sufficient to constitute a cause of action against defendant Bonding Company, and the trial court erred in overruling defendant's demurrer thereto and in refusing to find judgment for the defendants."

An examination of the eight specific assignments grouped under these two "Points" and the argument of counsel in support thereof (Br. pp. 53-74) disclose that the contention made by plaintiff in error is:

"That a cause of action was not pleaded; that the facts found did not sustain the judgment; that the evidence does not sustain the judgment, and that the judgment is against the law and the facts of the case."

Because the two questions which we concede may be urged under the writ are here involved in their entirety, the two points of the plaintiff in error have been discussed at greater length than might otherwise be justified.

The Facts Involved Under Points I and II.

The alleged insufficiency of the pleadings and proof, as we conclude from an analysis of the argument of plaintiff in error (Br., pp. 53-73), is ascribed to the fact that the proceeds of the 1091 bales of cotton, disposed of by Sears in violation of the terms of the trust agreement and misapplied to the payment of losses incurred by him in the transaction of the business of the Cotton Company instead of in the redemption of the trust receipts, fails to indicate any loss of money or personal property of the Cotton Company including that for which it may be responsible to others.

The court found. and the correctness of the findings are not challenged, that between November 19, 1920, and April 25, 1921, Sears, with the intent then and there entertained by him of dishonestly misappropriating and wilfully misapplying the warehouse receipts, the cotton represented thereby and the proceeds obtained therefrom, and with the fraudulent intent of causing a loss to the Cotton Company of its money and personal property for which it would be and has become responsible to the plaintiff Bank, applied to and secured from the plaintiff Bank the warehouse receipts then in its possession [Finding No. 6, Tr. p. 128]; and as a part of said transaction delivered the trust receipts in question [Tr. p. 129], explaining the necessity for the surrender of the receipts in order to make sales of the cotton, promising upon the exchange of the warehouse receipts for bills of lading to return the bills of lading and take up the warehouse receipts [Tr. p. 130].

That during this time and pursuant to said fraudulent and dishonest plan and scheme entertained by him, Sears surrendered the warehouse receipts obtained from the plaintiff Bank, sold the cotton represented thereby and received from the common carriers bills of lading therefor, and immediately thereafter, in violation of his promises and representations to the plaintiff Bank and in violation of the terms of the trust receipts, but pursuant to the dishonest plan and scheme entertained by him, Sears prepared sight drafts upon the parties to whom he had sold the cotton, attached the bills of lading thereto, and thereupon presented the sight draft, bill of lading attached, to an officer of the plaintiff Bank other than the officer from whom Sears had obtained the warehouse receipts and to whom he had delivered the trust receipts, and represented to such officer to whom the sight drafts were presented that the cotton covered by said sight drafts and bills of lading was cotton belonging to the Cotton Company and wilfully failed to disclose to said officer that the plaintiff Bank then held trust receipts of the Cotton Company given by said Sears covering said cotton described in said bills of lading attached to said sight drafts [Finding No. 7, Tr. pp. 131-132]. That having secured the approval of said officer (which authorized the teller to accept the sight draft as a cash deposit and not for collection [Tr. p. 133], Sears deposited the sight draft and bill of lading and secured a cash credit entry) upon the bank pass book of the Cotton Company, in the amount of the sight draft, and immediately thereafter, pursuant to his fraudulent

scheme, falsified the books of the Cotton Company by entering therein the various amounts of the sight drafts and carrying these upon the books of the Cotton Company as credit items without limitation of any kind and wilfully failed to enter any memorandum or book entry showing that the warehouse receipts had been secured by the issuance of trust receipts, or that trust receipts had been issued, or that moneys and credits entered in the bank pass book were received by the sale of cotton covered by trust receipts held by the bank, and failed to make any entry indicating that the money shown in the cash account was other than absolute and unencumbered funds of the Cotton Company [Tr. pp. 133-134]. That Sears, pursuant to his fraudulent and dishonest plan and scheme, during said time represented to the officers and directors of the Cotton Company that the various sums of money and credits entered upon the bank pass book and the books of account of the Cotton Company were moneys of said Cotton Company made and accumulated by Sears in the conduct of its affairs, and upon inquiry made of him represented to the officers of the plaintiff Bank that the Cotton Company still retained, and that he as its secretary still had in his custody in the vaults of the Cotton Company, all the warehouse receipts surrendered to him by the plaintiff Bank [Tr. pp. 134-135]. That the directors and officers of the Cotton Company and of the plaintiff Bank believed, acted upon and were deceived by the dishonest and fraudulent representations and statements of Sears [Tr. p. 135].

That Sears, pursuant to his fraudulent and dishonest plan and scheme, and contemporaneously with the several fraudulent and dishonest conversions and misapplications of the warehouse receipts and cotton represented thereby and the moneys and credits realized therefrom, and pursuant to the false and fraudulent representations made and deceits practiced by Sears upon the Cotton Company and the plaintiff Bank, Sears, continuing to act as secretary of the Cotton Company, fraudulently and dishonestly misappropriated and wilfully misapplied the moneys and funds placed to the credit of the Cotton Company following the various dishonest and fraudulent sales of cotton and disposition of warehouse receipts as hereinbefore mentioned by using said moneys and funds for the purpose of dealing and speculating in cotton in the name of the Cotton Company, conducting such speculations at a loss and paying said losses out of said moneys and funds, and in the payment of claims and demands incurred by Sears in such dealings and speculations in cotton [Finding No. 8, Tr. pp. 135-136]. That relying entirely upon the false and fraudulent representations of Sears as herein mentioned and the deceits practiced by him upon them, the directors and officers of the Cotton Company continued the business of the Cotton Company and consented to Sears, subsequent to the 19th day of November, 1920, continuing to act as secretary of said Cotton Company and to deal and speculate in cotton and to incur indebtedness and contract financial obligations in connection therewith upon its behalf. That said Cotton Company, its directors

and officers, would not have consented to the continuing of the business of the Cotton Company subsequent to the 19th day of November, 1920, neither would they have consented to Sears continuing to act as secretary after said date, neither would they subsequent to said date have consented to Sears conducting any dealings or speculations in cotton nor incurring any indebtedness or contracting any financial obligations upon its behalf had it or its directors or officers, other than said Sears, known of the frauds and deceits, or any of them, being practiced upon said Cotton Company and said plaintiff Bank by said Sears as hereinbefore mentioned [Tr. pp. 137-138]. That because of the frauds, deceits and dishonesty so perpetrated by Sears, said Cotton Company has sustained a loss and has become and is responsible to the plaintiff Bank in an amount in excess of the penalties of the bond [Finding No. 9, Tr. p. 138].

The Law Involved Under Points I and II. Construction of Terms of Bond.

(a) Fidelity bonds of a surety company are construed most strongly against the surety and in favor of the indemnity, and wherever a bond is fairly open to two constructions, one of which will uphold and the other defeat the claim of the insured, that which is the more favorable to the insured will be adopted.

1. 21 R. C. L. p. 1160, Sec. 200.

> "200. Measure of Liability.—The law of suretyship has undergone a considerable change in late years. The day of personal suretyship is fast

slipping away, and in its stead comes the corporate surety for profit. Formerly, a surety was an individual, or collection of individuals, actuated by beneficient motives to carry the burden of the suretyship, receiving no profit or benefit, and, in consequence thereof, the law dealt tenderly with him or them. But, in this day and age of corporate sureties, the burden is lightened by the payment of adequate premiums, and their final liabilities are oft-times secured by counter indemnity. As a result of this new condition of affairs the trend of all modern decisions, federal and state, in the construction of the law appertaining to sureties is to distinguish between individual and corporate suretyship, where the latter is an undertaking for money consideration by a company chartered for the conduct of such business. In the one case, the rule of *strictissimi juris* prevails as it always has, that is, the contract of an individual surety, or a 'voluntary surety' as he is spoken of in some cases, will be strictly construed and all doubts and technicalities resolved in favor of the surety, such person being regarded as a favorite of the law. But in the other case, because *it is essentially an insurance against risk*, underwritten for a money consideration by a corporation adopting such business for its own profit, the contract will be construed most strongly against the surety and in favor of the indemnity which the obligee has reasonable grounds to expect. And, in general, as the contracts of surety companies are essentially contracts of indemnity, the courts ordinarily apply to them by analogy the rules of construction *applicable to contracts of insurance*. Hence, *in an action on a bond written*

by a surety company, if the bond is fairly open to two constructions, one of which will uphold and the other defeat the claim of the insured, that which is most favorable to the insured will be adopted. Moreover, the courts generally hold that such a company can be relieved from the obligation for suretyship only where a departure from the contract is shown to be a material variance, or, as it has been otherwise expressively stated, the modern day surety company must show some injury done before it can be absolved from the contracts which it clamors to execute. For, it has been said, to allow such companies to collect and retain premiums for their services, graded according to the nature and extent of the risk, and then to repudiate their obligations on slight pretexts that have no relation to the risk, would be most unjust and immoral and would be a perversion of the wise and just rules designed for the protection of voluntary sureties."

2. 32 Cyc. p. 306, par. E;

3. Amer. Surety Company v. Pauly, 170 U. S. 133.

"If, looking at all its provisions, the bond is fairly and reasonably susceptible of two constructions, one favorable to the bank and the other favorable to the surety company, *the former,* if consistent with the objects for which the bond was given, *must be adopted,* and this, for the reason that the instrument which the court is invited to interpret was *drawn by the attorneys,* officers, or agents of the surety company. This is a well established rule of the law of insurance. National Bank v. Insurance Co., 95 U. S. 673; Western Ins. Co. v. Cropper, 32 Penn. St. 351, 355;

Reynolds v. Commerce Fire Ins. Co., 47 N. Y. 597, 604; Travelers' Ins. Co. v. McConkey, 127 U. S. 661, 666; Fowkes v. Manchester etc. Life Ass'n., 3 Best & Smith, 917, 925. As said by Lord St. Leonards in Anerson v. Fitzgerald, 4 H. L. Cas. *484, *507, 'it (a life policy) is of course prepared by the company, and if therefore there should be any *ambiguity* in it, must be taken, according to law, *most strongly against the person who prepared it.*' There is no sound reason why this rule should not be applied in the present case. The object of the bond in suit was to indemnify or insure the bank against loss arising from any act of fraud or dishonesty on the part of O'Brien in connection with his duties as cashier, or with the duties to which in the employer's service he might be subsequently appointed. *That object should not be defeated by any narrow interpretation of its provisions, nor by adopting a construction favorable to the company if there be another construction equally admissible under the terms of the instrument executed for the protection of the bank.*" (p. 144.)

4. U. S. F. & G. Co. v. Egg Shippers F. & S. Co., 148 Fed. p. 353 (Circuit Court of Appeals, 8th Circuit);

5. Champion I. M. & C. S. Co. v. American Bonding & Trust Co., 115 Ky. 863, 75 S. W. 197.

"It will be observed that the bond in this case is a *printed one*—prepared, doubtless, by a skilled attorney in appellees' employ. The contract expressed therein is but a *form of insurance,* and the law of insurance is that, in the construction of policies, if there be any *ambiguity* in them, it must

be considered *most strongly against the insurance company.* In American Surety Company v. Pauly, 170 U. S. 133, 18 Sup. Ct. 552, 42 L. Ed. 977, Mr. Justice Harlan admirably states this rule." (p. 198.)

6. Remington v. Fidelity & Deposit Company of Maryland, 27 Wash. 429, 67 Pac. 989.

"The provisions in the contract above quoted are for the protection of the insurance company. They were not intended to avoid an existing liability under the contract or as a means of defeating recovery thereon, but *only to prevent further liability* after discovery of dishonesty by the employer. *For such purpose, the provisions are reasonable and will be maintained, but if they are to be considered as a shield to avoid a liability legally and rightfully due, or to avoid a contract properly made, they are a fraud upon the rights of the insured, and cannot be upheld.* The words 'The employer shall immediately give notice to the company' should receive such interpretation as not to fritter away the substantial rights of the parties, nullify the contract, or promote fraud." (pp. 991-2.)

7. Title Guaranty & Surety Company v. Bank of Fulton, 89 Ark. 471, 117 S. W. 537.

"In order to determine whether these statements are warranties or mere representations, it is necessary to consider the nature of the bond sued on and what construction the law makes relative to the provisions of such bonds. This is not an ordinary obligation given by a surety, but it is an indemnity bond and is in the nature of a *contract of insurance, insuring the fidelity of the employe.*

It is said by this court in American Bonding Co. v. Morrow, 80 Ark. 49, 96 S. W. 613: 'It is now well settled that the bond of a surety company, like any other insurance policy, is to be *most strongly construed against the insurer.* The language of the bond is that *selected and employed by the insurer,* and when doubtful or *ambiguous must be given the strongest interpretation against the insurer which it will reasonably bear.'* And so in determining the nature of the provisions of this bond, we first look to see whether the provisions are susceptible of two constructions. If they are, then *we must adopt that construction which is most favorable to the bank.* This is the well settled doctrine as to the construction of such instruments as the bond sued on in this case. American Surety Co. v. Pauly, 170 U. S. 133." (p. 540.)

(b) The dishonesty covered by the bond of fidelity insurance need not be acts constituting a crime and punishable as such.

1. United States v. Northway, 120 U. S. 327.

"The offense of wilfully misapplying the funds of a banking association, as defined by the statute, was considered with reference to the facts in that case. It was there held that a wilful and criminal misapplication of the funds as defined by Sec. 5209, *did not include every case of an unlawful application of funds,* inasmuch as in the very statute itself there were other instances of unlawful misapplication evidently not embraced within the intention of Sec. 5209. For that reason it was held, in that case, that it was necessary to specify the particulars of the application, *so as to distin-*

guish that charged in the indictment as wilful and criminal from those others contemplated by the statute which are unlawful but not criminal." (p. 332.)

2. Citizens Trust and Guarantee Company v. G. & R. F. Insurance Company, 229 Federal, 326 (Circuit Court of Appeals, 4th Circuit);
3. U. S. F. & G. Co. v. Egg Shippers F. & S. Co., 148 Federal, 353 (C. C. A., 8th Circuit);
4. City Trust Company v. Lee, 204 Ill. 69, 68 N. E. 485;
5. Rankin v. U. S. F. & G. Co., 99 N. E. 314, 86 Ohio St. 267.

(c) To justify a recovery under a bond indemnifying an employer against loss by reason of the fraud or dishonesty of an employee, it is not necessary to show that the acts complained of resulted in profit to, or were calculated or intended to result in profit to, the employee.

1. U. S. F. & G. Co. v. Egg Shippers F. & S. Co., 148 Fed. 353 (C. C. A., 8th Circuit).

"The test is not whether he intended to personally profit by his course, though that he did is perhaps a permissible inference from the facts shown. He occupied a position of trust and confidence which he secretly betrayed. He received compensation for guarding the interests of his employer and he was wilfully, intentionally and grossly faithless. *This is not a case of mere indiscretion or error of judgment. There was a breach of trust, a want of financial integrity*

coupled with deceit and concealment, and resulting in financial loss to the employer. This was both fraud and dishonesty within the meaning of the bond. Cases involving fidelity bonds insuring against 'embezzlement and larceny' or 'fraud and dishonesty amounting to embezzlement or larceny' are obviously not in point." (148 Fed. 355.)

2. Rankin v. U. S. F. & G. Co,, 99 N. E. 314, 86 Ohio St. 267;
3. Roseville Trust Company v. American Surety of New York, 91 N. J. Law 558, 103 Atlantic 182

(d) By the term "wilfully" is meant purposely or designedly. The intent to injure and defraud, which is necessary to constitute a wilful misapplication, does not necessarily involve any malice or ill will but merely that general intent to injure and defraud which always arises in contemplation of law when one wilfully and intentionally does that which is illegal or fraudulent and which in its necessary and natural consequences must injure another.

1. Agnew v. United States, 165 U. S. 36;
2. Walsh v. United States, 174 Federal 615 (C. C. A.);
3. Pearce v. United States, 192 Federal, 561 (C. C. A.).

(e) Where a clause of the bond is being construed all the language and not merely a portion thereof must be taken into consideration.

1. Kansas Flour Mills Company v. American Surety Company, 98 Kansas 587, 158 Pac. 1118;

2. Campbell v. Maryland Casualty Co., 52 Ind. App. 228, 97 N. E. 1026.

(f) To constitute a wilful misapplication even in criminal cases it is only necessary to show the acts complained of were performed purposely and designedly.

1. Pearce v. United States, 192 Fed. 561 (C. C. A.)

Discussion.

1. Under the terms of the bond, the Maryland Casualty Company agreed that it would

> "reimburse the employer for any loss * * * of money, securities or other personal property (including that for which the employer may be responsible to others) which the employer shall have sustained by reason of any act or acts of fraud, dishonstey, forgery, embezzlement, wrongful abstraction or wilful misapplication on the part of the employee while in the performance of his duties as secretary. * * *"

Excluding from consideration the parenthetical phrase, it is our contention that the Cotton Company has sustained a *loss* within the restricted and technical meaning of the word in this: that securities—cotton tickets—to the number of 1091 have been lost to the Cotton Company through Sears' lack of fidelity. The loss is shown by the following facts: The cotton was purchased and paid for by the Cotton Company. The money was furnished by the bank in the nature of a loan upon acceptances secured by cotton represented by warehouse tickets. Had Sears been faithful to his trust, the cotton tickets on May 1, 1921, would have

been in Sears' possession or on deposit with the Citizens National Bank, attached to the 87 acceptances, *or* they would have been exchanged for bills of lading and the bills of lading would have been in the possession of the Citizens National Bank, *or* the bills of lading having been returned to the Citizens National Bank and the trust receipts taken up, pursuant to Sears' agreement and the terms of the trust receipt, the Citizens National Bank would have forwarded sight drafts, bills of lading attached and received the money upon the delivery of the cotton, applied the same to the acceptance account and in this way there would have been no loss of cotton tickets. In other words, had Sears dealt honestly with the Cotton Company and the bank he could not have disposed of the 1091 bales of cotton to which the Bank and Cotton Company looked as security for the acceptance account. Due to Sears' perfidy, the Cotton Company has lost its cotton and the bank has lost its security.

Counsel for plaintiff in error contends, however, that inasmuch as the proceeds from the wrongful disposition of the cotton was credited to the Cotton Company on its books and upon the books of the bank, and inasmuch as the money was thereafter expended by Sears in the business of the Cotton Company (overdraft eliminated), the Cotton Company has sustained no loss. (Brief pp. 55, 56, *et seq.*)

The answer to this suggestion is that the evidence discloses that the indebtedness of the Cotton Company which was paid by Sears from the funds realized from the wrongful disposition of the cotton was indebted-

ness which would not, and could not have been incurred had he been faithful to his trust. This is not a case where the Company has two enforcible claims to meet and the employee applies funds intended for the satisfaction of one claim to the satisfaction of the other; this is an instance where the company has one enforcible claim to meet and has sufficient collateral deposited to insure the payment thereof and the employee practicing a series of frauds and deceptions incurs in the name of the company (he having the power so to do), another claim against the company (which could not have been incurred but for his duplicity) and fraudulently obtains and disposes of the collateral and uses the funds realized therefrom to extinguish the liability by him fraudulently incurred.

Coming now to a consideration of the parenthetical phrase, towit, "including that for which the employer may be responsible to others" [Tr. p. 205]. It is elementary that in the construction of any form of contract the courts will consider that language used was intended for a purpose and will not presume that the language was intended to be meaningless, or was inserted without reason therefor. In Maryland Casualty Company etc. v. Bank of England, 2 Fed. (2d) 793, at 795, 796, cited by plaintiff-in-error on another point (Br. p. 111), the court said: "Other rules of construction are that all parts of a contract must be given a reasonable meaning and vitality, and that parties are presumed not to insert idle, foolish, meaningless language." The language in question (parenthetical phrase) is inserted in the most important

sentence of the bond, and the courts will not conclude that it was inserted inadvertently and without the intention of including that which otherwise would not be included. We feel that it would be difficult to use language more clear or concise than that set forth in the parenthetical phrase in order to extend the scope of the term "loss of personal property" to circumstances where the fraud of employees imposed a responsibility upon the employer.

In a South Dakota case (Farmers & Merchants Bank v. U. S. F. & G. Co., 28 S. D. 315, 133 N. W. 277 (37 L. R. A. [N. S.] 1153), *afterward overruled upon another point* (manipulation of stock), the court announced the proposition we declare elementary as follows:

> "It must be presumed that the clause was designed to effect the rights of the parties under the contract; to either enlarge or restrict the defendant's liability as defined by the general terms of its undertaking."

The case of Campbell v. Maryland Casualty Company, 52 Ind. App. 228, 97 N. E. 1026, is decidedly applicable to the question under discussion. The action was instituted to recover on an employer's liability policy of insurance issued to a stone company; later, with the consent of the obligor, consigned to a second stone company. The action is by the receiver of the second stone company. A judgment was obtained against the assignee by an employee, personal injury having been received by him in the line of his employment. Before the judgment in the

personal injury action was affirmed on appeal, the assignee stone company became insolvent and passed into the hands of a receiver. The policy of insurance provided that the—

> "obligor agrees to indemnify the assured * * * against loss * * * on account of bodily injuries * * * suffered by an employee of the assured while on duty caused by the negligence of the assured."

On the reverse side of the policy, the following provision was printed:

> "8. *No action shall lie* against the company as respects any loss under this policy unless it shall be brought by the assured himself to reimburse him for *loss actually sustained* and *paid* by him in *satisfaction of a judgment* after trial on the issue."

Respecting this provision, the court said:

> "The language quoted from the body of the policy, as well as the language of the provision No. 8 heretofore set out, would seem to indicate that the purpose of the contract was to indemnify the assured against loss and not to protect it against liability."

Discussing the same matter, the court states:

> "If the policy sued on is a contract to indemnify against loss, it is necessary to show a damage before there can be a recovery (citing cases). *On the other hand,* if the policy sued on is a contract to protect the assured against liability merely, an action may be brought and a recovery had *as*

> *soon as the liability is legally imposed,* regardless of the question as to whether or not any actual loss or damage has been suffered (citing cases). The distinction observed between contracts to indemnify against loss and contracts to protect the assured against liability is recognized by practically all the cases cited." (Page 1027.)

Attached to this policy was a slip or rider which contained the following provision:

> "This policy shall only cover losses sustained by and liability for any claims against the assured as a result of the risk specified in the contract * * *."

Concerning this language of the rider, the court said:

> "This slip seems to have the effect to so *modify* the body of the policy and condition No. 8 as to make the policy cover not only losses sustained by the assured, but *also liabilities* for any claims against the assured. If the language of the slip is to be given any meaning at all, it must have the effect stated; *and it certainly will not be presumed* that the parties took the trouble to attach a slip to the policy *without intending* thereby to *change its effect.* By virtue of the slip, the policy sued on was made to cover liabilities against the assured as well as losses. The plaintiff may recover upon this policy under the authority of the cases cited without showing an actual loss. It is sufficient if he show that a liability has become legally fixed."

This case also announces the rule we have heretofore styled as elementary in the construction of fidelity bonds to the effect that a parenthetical clause must be presumed to have been intended for some purpose and not idly nor meaninglessly inserted. The court declares:

> "If the contract in question were to be construed solely from a consideration of the provisions heretofore referred to and in the light of the authorities cited, we should have no doubt as to its meaning; but the policy in this case carries a slip or rider, which, to the mind of the court, materially affects its meaning. * * * *In attaching this slip* to the policy, the parties no doubt intended *to modify in some manner* the force and effect of the language of the policy. * * * If the language of the slip is to be given any meaning at all, it must have the effect stated; and it certainly will not be presumed that the parties took the trouble to attach a slip to the policy without intending thereby to change its effect." (p. 1028.)

An Oregon case cited in the opinion of the Indiana court, towit, Fenton v. Fidelity & Casualty Co. of N. Y., 36 Ore. 283, 56 Pac. 1096, is to the same general effect as the Indiana case. The Oregon court applies *to the interpretation of the provision of the policy covering loss or liability,* the rule we have so frequently referred to:

> "If, however, the meaning of the policy is in doubt, and its language is fairly and reasonably susceptible of two constructions, one favorable to the assured, and the other to the defendant, the

> one is to be adopted which is the most favorable to the assured. This is the universal ruling in the construction of insurance policies, because they are drawn by the attorneys, officers, and agents of the company; and it is but fair that, if there should be any ambiguity or uncertainty in the language used, it should be construed most strongly against the company." (56 Pac. p. 1098.)

The Cotton Company, because of Sears' lack of fidelity sustained a loss of personal property consisting of 1091 bales of cotton and by reason thereof has become responsible to the Citizens National Bank in an amount in excess of the defendant's liability under the terms of the bond. What would have occurred had Sears been faithful to his trust is in many respects a matter of conjecture. What has resulted from his faithlessness is disclosed by the testimony. The testimony discloses that, had the directors of the corporation known on November 19, 1920, of Sears' fraudulent scheme to carry on the business, the consummation of the plan would have been prevented.

Plaintiff in error at page 56 of its brief submits a hypothetical case which it alleges is analogous to the case now before the court. We submit that there is entirely lacking in the illustration of plaintiff in error the controlling factor in the case now before the court. If Sears' transactions had stopped after the sale of the cotton and the deposit of the sight draft bills of lading attached as a cash item to the credit of the Cotton Company, and at the time of his suicide there had been standing to the credit of the Cotton Company in the bank all of the moneys realized from the sale or con-

version of the cotton, then the situation would have been analogous to the example submitted by plaintiff-in-error. Sears' perfidy, however, did not cease upon securing the cash entries to the credit of the account of the Cotton Company. He thereafter dishonestly dissipated these funds so that at the time of his suicide the Cotton Company was without the cotton or the proceeds realized from its sale to meet the liability incurred upon the acceptances.

For the consideration of the court, we suggest the following illustration:

Assume that on the 19th day of November, 1920, the Cotton Company had on deposit with the Citizens National Bank $75,000.00 accumulated in previous years' business, and carried in a special account. On this date Sears discovers that he has no money in his checking account to operate the business and that the only assets of the company other than its furniture, fixtures and going concern value is the $75,000.00 in the special account. On this day a sight draft drawn upon the Cotton Company, attached to which are certain cotton tickets, arrives at the Citizens National Bank and Mr. Sears is informed of its arrival. Mr. Sears then states to the directors of the company: "Let us go and accept this sight draft, take out the cotton tickets, substitute our trust receipt, represent to the bank that upon the sale of the cotton we will return a bill of lading covering the shipment, but when we make a sale of the cotton and secure a bill of lading, we will attach thereto a sight draft drawn upon the purchaser thereof, put the matter through

the bank as a cash transaction; check out the money and use it to run the business."

Of course, the suggestion, according to the testimony of all the witnesses, would have met with their disapproval. They would not have allowed any such conduct on Sears' part. It is only reasonable to assume that Sears knew that the directors would not allow him to work any such fraud upon the bank, making them and the company liable therefor. Instead of taking the matter up with the directors, Sears, however, reflects with himself as follows: "Well, I will not tell the directors of my scheme. I will keep the matter to myself." But he does say to the directors, on the 19th day of November, 1920, and frequently thereafter,— "We are making money in the conduct of this business," and he continues the business, and by the first of May, 1921, he has withdrawn 1091 cotton tickets from the bank, substituting trust receipts therefor, spends the money in conducting the business, but in a manner and for purposes which the directors would not have permitted had they known the facts. On May 19, 1921, the bank being informed of Sears' lack of integrity, withholds (Calif. Civil Code, sec. 3054) $60,000.00 of the $75,000.00 (special account), being the value of the cotton tickets wrongfully obtained and converted. In this instance the Cotton Company has lost $60,000.00 through Sears' duplicity. In other words, if Sears had told the directors of the corporation what he expected to do; if he had told them of the fraudulent plan under which he was going to operate, they would have stopped the fraud in its inception;

but he didn't tell them,—he went ahead and perpetrated his deceits upon all concerned, the bank and the Cotton Company, deceived them both as he proceeded, and during that time when he was perpetrating his fraud and practicing his deceit and duplicity he caused a loss to the Company of $60,000. The Company has lost that money,—they have become responsible to the bank for that amount, and the bank has taken that amount from their special account. That is the manner in which Sears' duplicity and dishonesty has resulted in a loss and caused the Company a liability, or has imposed upon it a responsibility to the bank. In other words, if Sears had told the truth; if he had conformed his conduct to his representations, such a situation would never have arisen. Because of his duplicity, however, a situation arose which put the Cotton Company in a position where they are required to pay the bank an amount of money, and the source (cotton tickets) relied upon by the Cotton Company to obtain this money, because of Sears' duplicity has vanished.

We conclude this subdivision of our brief by a quotation from the opinion of the learned judge of the trial court [Tr. pp. 179-180]:

"When the cotton market became disturbed and the business as conducted by Sears began to show a loss on purchases and sales, Sears failed in his duty to the bank. After withdrawing cotton tickets or warehouse receipts, and carrying through his sale of the particular cotton, he, in a great many instances, numbering well toward one hundred, failed to replace the withdrawn tickets by outbound documents, which resulted

in the end, in the bank being left with a debt of approximately $80,000.00 owing to it by the Cotton Company, which was not secured by collateral as the agreement contemplated. The act of Sears was more than a breach of faith; it approached an embezzlement of collateral in which the bank held a qualified property interest. It is argued on behalf of the defendant that the bad conduct of Sears in this regard caused no loss to the Cotton Company, against which only the indemnity had been furnished; that the misuse of the collateral did not cause the Cotton Company to lose what it already owed to the bank. And, furthermore, that whatever criticism might be made of the conduct of Sears, that all of the proceeds which he received were devoted to the business of the Cotton Company and not appropriated by the manager to his own or any other person's use. To my mind, that argument draws too narrow a line in the interpretation of the terms of the bond. The Cotton Company contemplated that its loan account would at all times be protected by collateral received in the usual and ordinary course of its dealings. The securities of the kind first described, when once they reached the bank, if removed under the shifting arrangement referred to, were property for which the Cotton Company was responsible and was bound to return in their resulting equivalent to the bank. The bank was entitled to demand and recover from the Cotton Company the agreed equivalent of the cotton tickets had the equivalent at any time been found in possession of the latter. The unauthorized use of the securities by Sears should be held to amount to a wilful misapplication of property for which the Cotton Company was responsible to the bank. Sears' breach of faith did result in a loss to the Cotton Company, because it would add to its liabilities

the value of the collateral illegally withheld by Sears and used without authority in the business."

Point of Plaintiff in Error No. III Answered.

Assignments of error numbers 11 and 26 are by plaintiff in error grouped under the heading:

III.

"There is no evidence to support or justify the findings of the trial court as set forth in finding No. VII that the reasonable value of the 1091 bales of cotton sold and disposed of by the Cotton Company, and for which the plaintiff bank held trust receipts was *at the time the same were sold and disposed of,* of the reasonable value of $60,594.62, or to support finding No. XXIV that the 455 bales of cotton covered by warehouse receipts delivered by plaintiff bank to the Cotton Company prior to December 1, 1920, and not returned to the bank were *at the time they were sold and disposed of,* of the reasonable value of $29,336.99." (Br. pp. 49-50.)

The Facts Involved Under Point III.

We have italicized the phrase *"at the time they were sold and disposed of"* because of the fact that it is a radical departure from the findings. Finding No. VII [Tr. p. 135] is to the effect that the 1091 bales of cotton disposed of by Sears as set forth in the findings *"were at the time of such fraudulent and dishonest conversion"* of the value of $60,594.62. Finding No. XXIV [Tr. p. 153] is to the effect that the 455 bales of cotton covered by warehouse receipts delivered by plaintiff bank to Sears prior to December 1, 1920, and not returned to the bank *"at the time of their delivery*

by *said plaintiff to said J. B. Sears,*" were of the reasonable value of $29,337.99 [Tr. p. 153].

The court found:

"That at various times * * * between said 19th day of November 1920, and said 25th day of April, 1921, and in most instances *immediately following* the acceptance of each of said sight drafts * * * with the intent then and there by him entertained of fraudulently and dishonestly converting, misappropriating, and wilfully misapplying said warehouse receipts, the cotton represented thereby and any money or proceeds obtained therefrom, and with the further fraudulent and dishonest intent then and there by him entertained, of thereby causing a loss to said California Cotton & Factorage Company of money, securities and personal property for which it would be, and has, become responsible to the plaintiff herein, said J. B. Sears applied to, and secured from the plaintiff the warehouse receipts then in its possession, * * *." [Finding No. 6, Tr. p. 128.]

"That at said time, and as a part of the same transaction * * * Sears executed and delivered * * * eighty-seven (87) of said trust receipts * * * [Tr. p. 129.] That * * * *pursuant to said fraudulent and dishonest plan and scheme* said J. B. Sears at various times and irregular intervals procured from the plaintiff herein between the 19th day of November, 1920, and said 25th day of April, 1921, fourteen hundred and seventy-six (1476) warehouse receipts * * * and issued and delivered to the plaintiff, in acknowledgment thereof, eighty-seven (87) of said trust receipts." [Tr. p. 130.]

"That subsequent to said 19th day of November, 1920, * * * said J. B. Sears, *pursuant to said*

fraudulent and dishonest plan and scheme by him entertained as hereinbefore found, fraudulently and dishonestly converted, misappropriated, and willfully misapplied ten hundred and ninety-one (1091) of said * * * warehouse receipts and ten hundred and ninety-one (1091) bales of cotton represented thereby in the manner following, that is to say:" (Here follows recital of the manner in which Sears having obtained the warehouse receipts sold the cotton covered thereby, surrendered the warehouse receipts and obtained possession of the bills of lading.) [Finding No. 7, p. 131.]

"That said J. B. Sears immediately thereafter, in violation of his duties as secretary * * * and in violation of his promises and representations to the plaintiff, and in violation of the terms of said trust receipts * * * *but pursuant to said fraudulent and dishonest plan and scheme*" (Here follows recital of fraud and deceit practiced by Sears in presenting a draft with bill of lading attached to officers of the bank not acquainted with Sears' transaction with the note department, the securing of approval thereof, the depositing of the same as a cash item, the securing of cash deposit entries upon the bank pass book, the falsification of the books of account of the Cotton Company to disguise and cover up the fraudulent transactions and the subsequent fraudulent and dishonest representations to the officers of the Cotton Company and the bank respecting the making of money by the Cotton Company and the holding of all the Cotton tickets covered by the trust receipts in the possession of the bank, and the belief, reliance and action by the officials of the Cotton Company in the bank upon such fraudulent and dishonest representations.) [Tr. pp. 132-135.]

The evidence discloses [Stipulation, Tr. p. 432]:

"That upon the death of said J. B. Sears said California Cotton & Factorage Company did not have in its possession and did not thereafter surrender to said Citizens National Bank ten hundred ninety-one (1091) of said fourteen hundred and seventy-six (1476) warehouse receipts; that said ten hundred ninety-one (1091) bales of cotton represented thereby cost said California Cotton & Factorage Company *at the time of their purchase* and *were then of the value* of sixty thousand five hundred ninety-four 62/100 dollars ($60,594.62)."

The evidence also discloses [Stipulation, Tr. pp. 431-432]:

That the four hundred fifty-five (455) bales of cotton covered by warehouse receipts delivered by plaintiff bank to Sears prior to December 1st, 1920, and not returned to the bank *cost* the Cotton Company and *at the time of their purchase were of the value* of twenty-nine thousand three hundred and thirty-seven dollars ninety-nine cents ($29,337.99).

The Law Involved Under Point III.

The wrongful conversions by Sears date from the time of acceptance of the sight drafts and obtaining possession of the cotton tickets pursuant to the fraudulent and dishonest scheme then entertained and being perpetrated by him; and the value of the cotton tickets at that time, in the absence of any other evidence of value, is conclusive proof of the measure of damages recoverable by the defendant in error.

1. Sedgwick on Damages (9 ed.), Vol. 2, Sec. 497, p. 964.

"Upon general principles, the value of the property at the time of conversion should be the measure of damages, and that is the rule generally adopted."

2. Sutherland on Damages (4 ed.) Vol. 4.

(a) Section 1112, p. 4222.

"Nothing appearing to the contrary, the date of conversion is presumed to be that at which the property was taken into the possession of the wrongdoer."

(b) Section 1113, p. 4223.

"In case of the exercise by a lienor of dominion over property where neither the date of the conversion nor the condition of the property at that time is shown, the damage may be proved by showing its value when it came into his possession. If the difficulty of proving value is very great and is the result of the defendant's act, he will not be relieved from liability on account thereof."

"If a bailee's promise is to deliver property valued in his receipt for it at a specified sum he is bound thereby, and if a portion of it is taken from him by process of law he must account for the difference between the value of the whole and of the remainder, regardless of the actual worth of the latter."

(c) Section 1132, p. 4273.

"The maker of notes which are diverted from their purpose may recover the amount it costs him to discharge them."

(p. 4277.)

"One who converts a written instrument payable by its terms to himself, but in which another has an interest, must account to the latter for his share of the full sum due according to the face thereof unless he shows its actual value."

(d) Section 1171, p. 4388.

"Following the principle that the recovery should be commensurate with the injury, if one is fraudulently induced to enter into a contract or pursue a course of action from which expenditures have naturally succeeded or in consequence of which he has been compelled to pay money or devote his time, the expenditures, with interest thereon, * * * will be elements of damage."

3. 8 Ruling Case Law, p. 489, (Damages Sec. 49).

"Generally the value of property taken or destroyed is to be determined as of the time and place of its taking or destruction."

4. 8 Cal. Jur. p. 907 (Sec. 140 Damages).

"It has been held repeatedly that evidence of the cost of property of which one has been wrongfully deprived is admissible as a circumstance tending to show its value. While such testimony may have slight probative value only, it may nevertheless be sufficient, in the absence of any counter testimony, to sustain a finding as to value."

5. California Civil Code, Section 3336.

6. Anderson v. United States (C. C. A. 9th Cir.) 152 Fed. 87, at 91.

7. Angell v. Hopkins, 79 Cal. 181, 183.

"It is quite true that the measure of damages is the value of the property at the time of the conversion with certain additions in certain cases. (Civ. Code, Sec. 3336.) But in arriving at such value, it was proper to take into consideration what the property cost as a circumstance, to aid at arriving at its value at the time in question. (Citing cases)".

Affirmed in

8. Greenbaum v. Taylor, 102 Cal. 624, 627;
9. Bacigalupi v. Phoenix Building etc. Co., 14 Cal. App. 632, 637;
10. Kirstein v. Berkins V. & S. Co., 27 Cal. App. 586, 589;
11. Union Hollywood W. Co. v. Los Angeles, 184 Cal. 535, 538;
12. Travis Glass Co. v. Ibbetson, 186 Cal. 724, 730.

Wilful Trespass Rule Applied in Federal Courts.

Where the original taking is dishonest or fraudulent, any subsequent act of the wrongdoer which *enhances* the value of the property cannot be permitted to enure to him.

1. Woodenwear Co. v. United States, 106 U. S. 432, 434;
2. Trustees of Dartmouth College v. International Paper Co., 132 Fed. 92, 95;
3. Beechwood Ice Co. v. American Ice Co., 176 Fed. 435, 437;

4. Providence M. & M. Co. v. Nicholson, 178 Fed. 29, 38;

5. Grant v. Fletcher, 283 Fed. 243, 265.

The court having found that Sears obtained the cotton tickets *pursuant to a dishonest scheme to convert and misapply them* and, the plaintiff in error having stipulated that at the time Sears obtained the tickets they had cost the Cotton Company and were then of the reasonable value found by the court, it would seem that the mere statement of these facts refutes the contention of plaintiff in error that there is no evidence to sustain the finding of the court respecting the value of the cotton converted. The argument of counsel for plaintiff in error upon this point is certainly not definite—there are no authorities cited—no principles announced. (Br. pp. 74, 75.) It would appear that their contention on this point is predicated solely upon testimony to the effect that cotton, during the second year, sold on an average of $12.00 per bale less than cost. This average is for all the cotton sold during the period of the second year [Tr. p. 436] which extended from November, 1920, until May, 1921, (Brief of Pltf. in Error, p. 12) consisting of the 1091 bales fraudulently obtained by Sears from the plaintiff bank as well as all other cotton coming into the hands of the Cotton Company from other sources, including cotton purchased through other banks and cotton purchased directly [Tr. p. 290] and for sales of this cotton occurring as late as April 25th, 1921.

This is no proof at all of what the 455 bales obtained by Sears from the plaintiff Bank prior to December 1st, 1920, were sold for.

Having in mind the rule of wilful trespass hereinbefore referred to and its application where the fraudulent conversion is followed by an *increase* in the value of the converted property, it would appear as a corollary thereto that any diminution in the value of the converted property should be borne by the wrongdoer. Indeed it would be a sad commentary upon the law under any system of enlightened jurisprudence to have it said that one may be dishonestly dispossessed of his property and his measure of damages for the conversion is determined not by the value of the property at the time of such conversion, but by such lesser value as the wrongdoer may later place upon it in consummating a sale thereof. The transactions of Sears subsequent to November 19, 1920, were by the court declared to be fraudulent and dishonest and conducted pursuant to a fraudulent and dishonest scheme.

However, the outstanding fallacy in the argument of plaintiff in error is the contention that the measure of recovery is the value of the cotton tickets *at the time the cotton was sold by Sears.* This is not the correct criterion to determine the liability of the Bonding Company. The liability of the Bonding Company is determined by the extent of the financial responsibility, for which by reason of the perfidy of Sears, the Cotton Company became liable to the Bank as of date of December 1, 1920. In other words, the Bonding Company agreed to reimburse the Cotton Company for

any loss—including the responsibility it incurred to others—by reason of the faithlessness of Sears. The extent of this liability is fixed by the value, *at the time of their conversion* of the 455 cotton tickets converted by Sears prior to December 1, 1920, which it was stipulated [Tr. pp. 431-432] cost the Cotton Company and which were then of the value found and determined by the court, viz: $29,377.99.

Point of Plaintiff in Error No. IV Answered.

Assignments of error numbers 2, 25, 27, 28, and 30 are by plaintiff in error grouped under the heading:

"IV.

The Cotton Company during the latter part of 1920 became a corporation sole—to-wit, J. B. Sears, and thereafter J. B. Sears, the 'risk' named in the bond, was in complete ownership and control of the Cotton Company. That on and after the date when such complete ownership and control was obtained by J. B. Sears the Cotton Company—to-wit, J. B. Sears, had no right of action to recover for any loss sustained by the wrongful acts of J. B. Sears, whether committed prior to or subsequent to the date on which the ownership and control of the Cotton Company was acquired by Sears. For that reason the trial court erred in finding judgment against defendant and in refusing to grant defendant's motion for judgment for defendant. In view of the finding of fact that the Cotton Company became a corporation sole—to-wit, J. B. Sears, on December 1st, 1920, the trial court erred in its conclusions of law that the plaintiff (assignee for collection of the Cotton Company) was entitled to judgment for any loss resulting from the wrongful acts of J. B. Sears." (Brief p. 76.)

The Facts Involved Under Point IV.

We contend that this point IV is for the first time raised under the writ of error. It was never submitted for the consideration of the trial court. As we read the assignments of error numbers 2, 25, 27, 28, and 30, specified as supporting the point, we conclude that no one or more of them raises the point now presented for the consideration of the appellate tribunal.

Let us examine the specifications of error noticed as supporting Point IV.

1. The first is assignment of error number 2. It specifies as error the overruling of the defendant's motion for nonsuit. In the first place, the record discloses [Tr. p. 377] that no exception was taken to the ruling of the court denying the motion. In the second place all of the evidence bearing on the stock transfer from West to Sears was introduced subsequent to the motion and as part of the defense of the plaintiff in error [Tr. pp. 379-402].

2. The second and fifth are assignments of error numbers 27 and 30. They specify the absence of evidence to support the finding that the stock transfer from West to Sears occurred December 1, 1920, and the failure to find that such transfer occurred prior to November 17, 1920. A consideration of the assignments involves an analysis of the evidence, and does not involve any question of law. These assignments are specifically attacked in Point V of plaintiff in error and the discussion of the assignments under that point as found in the brief of the plaintiff in error

(Br. pp. 95-101) is clearly distinct from and in no manner approaches the question set forth under Point IV now under discussion.

3. The third and fourth are assignments of error numbers 27 and 28. They specify as error the conclusion of the court that the plaintiff is entitled to judgment and the awarding of judgment in favor of plaintiff and against defendant on the ground that the same is contrary to the law, the cause made, the facts pleaded and the records in the action. These same assignments, viz: Nos. 27 and 28 are urged by plaintiff in error as supporting its points numbered I and VI, as well as No. IV (Brief pp. 49, 51). Points Nos. I and VI are fundamentally different one from the other and in their consideration by counsel for plaintiff in error involve essentially different matters of fact and law. (Brief pp. 53 to 66 and pp. 101 to 126.) As they differ one from the other, each of these points also differs from Point IV, and are so considered and presented in the brief of plaintiff in error.

Assignment of error No. 28 is an omnibus assignment clearly in violation of the rules of this court and the principles and practices of all courts requiring definiteness and particularity in the assignment of errors relied upon and intended to be urged.

In the fourth special defense pleaded by the plaintiff in error [Tr. pp. 79-81] it is alleged that West transferred his stock to Sears about May 24, 1920. This was long prior to the first conversions and misappropriations of Sears, which began November 19, 1920. [Pleading Tr. p. 40; findings Tr. p. 126.] The plain-

tiff in error contended before the trial court that the sale from Sears to West occurred about May 24th, 1920. This same contention is again made in this court. (Point V Brief pp. 95-100.) The defendant in error contended before the trial court that Sears never purchased the stock of West and that the title to the stock never passed to Sears. The court accepted the contention of neither party, but found that West sold the stock to Sears and that the title passed December 1, 1920 [Tr. p. 149]. There was never presented to the trial court the question which is now presented upon review. and we entertain very serious doubt whether the point as urged is proper under any of the assignments of error.

The Law Involved Under Point IV.

Plaintiff in error in its brief (pp. 81 to 95) has cited several authorities, quoting at length from some of them, upon a principle of law that has no application to the matter now before the court. Among these authorities are:

Meily Co. v. London etc. Fire Ins. Co., 148 Fed. 683 (Br. p. 95);

In re Rieger. 157 Fed. 609 (Br. pp. 93, 94);

Farmers & Merchants State Bank v. U. S. F. & G. Co. (S. D.), 36 L. N. S. 1152 (Br. pp. 89 to 92);

Frost on Guaranty Insurance (Br. pp. 85, 86, 87, 88, 89).

These decisions are authority for the proposition.

> "That the risk shall continue to occupy the position in the employ of the insured designated in the proposal or application for the policy."
>
> Frost, p. 346 (Br. p. 88).

Stating the same principle in the language of the opinion of the court in the South Dakota case cited:

> "The object of the undertaking was to insure an employer against the fraudulent acts of an employe, not to insure an employer against his own fraudulent acts. When the person whose conduct is insured ceases to be an employe within any fair and reasonable interpretation of the term used in the policy, the insurer's liability should cease, unless he has notice of the change."
>
> F. & M. State Bank v. U. S. F. & G. Co.. 36 L. N. S. 1152 (Br. p. 91).

Counsel for plaintiff in error states the principle in this fashion:

"A careful reading, however, of this later South Dakota decision does not in any way repudiate the rule announced in the earlier case that a substantial change of relationship between the employer and employe relieves the surety company from liability * * *." (Br. p. 92.)

The finding of the court [Tr. p. 149] is to the effect that on December 1, 1920, when West sold 496 of the outstanding 500 shares of stock to Sears that Sears thereafter became the practical owner, and for all practical purposes could be considered as the corporation, and as the direct consequence thereof the liability

on the part of the insurer under the bond ceased at that time and the amount of recovery was limited to the extent of the liability which had been incurred prior to December 1, 1920, or prior to the time that Sears ceased to be an employe and became the employer. To restate this simple matter, illustrating the lack of application of the principle announced in the preceding cases, we respectfully submit that the trial court applied the principle by refusing to allow any recovery for liability incurred subsequent to December 1, 1920, and limiting the recovery under the bond to the liability incurred while Sears acted in the capacity of general manager with the ownership of but one share of stock. Counsel for plaintiff in error make precisely this statement, at page 19 of the brief. It is as follows:

"The judgment rendered by the trial court * * * represents the amount paid by the plaintiff bank for the cotton * * * surrendered * * * prior to December 1, 1920 * * *."

Another principle which plaintiff in error advances is stated as follows:

"An unquestioned limitation on the insurer's liability is that the claim shall be a valid and enforcible one against the risk in favor of the insured." (Br. p. 82.)

Several authorities are cited in support of this proposition. We do not dispute that the principle is a correct one, but do dispute the unsupported statement of plaintiff in error that on December 1, 1920, the California Cotton & Factorage Company did not have an

enforcible claim against Sears. If the dishonesty and deception being practiced by Sears were discovered on that date there would have been not only a civil liability on Sears' part for his breach of faith but, as the trial court intimated [Tr. p. 179], a charge of embezzlement might with some justification have been made.

A third principle of law contended for by plaintiff in error and in support of which several authorities are cited may be stated as follows: If necessary to work out equitable ends or to prevent the perpetration of a fraud courts both at law and in equity will look bevond corporate entity to ascertain the real parties in interest. (Br. pp. 84, 85.) This principle is well and briefly stated by the Supreme Court of California in the recent case of Erkenbrecher v. Grant, 187 Cal. 7, at 9, 10, as follows:

> "While it is the general rule that a corporation is an entity separate and distinct from its stockholders, it is also equally well-settled that both law and equity will, when necessary to circumvent fraud, protect the rights of third persons, and accomplish justice, disregard this distinct existence and treat them as identical."

This principle was applied by the trial court in limiting the recovery under the bond to such liability as had been incurred prior to December 1, 1920, being the time when, as plaintiff in error contends, the employee became the employer, or the risk became the principal.

The real contention of counsel for plaintiff in error upon this point as we understand it (Brief, pp. 77-79) may be summed up in the following manner:

On December 1, 1920, the Bonding Company was liable to the Cotton Company in the amount specified in the judgment. On this date, however, Sears purchased the stock held by West, and thereafter, for all practical purposes, became the corporation and entitled to all its assets, one of which was the claim under the bond. If allowed to enforce this claim he would be benefiting by his own fraud. Consequently, the claim may not be enforced.

The first error of this reasoning is the assumption that the claim under the bond was assigned to Sears, another is that Sears got control of the stock of West. The fact is, that although the stock was issued in Sears' name and the court found West sold it to Sears, the stock was endorsed in blank by Sears and returned to West, who held it as collateral to secure the purchase price of the stock, no part of which was ever paid. [Tr. p. 388.] A third error in the argument is the assumption that if the judgment is paid by the Bonding Company it will benefit the wrongdoer, Sears, or his estate. The payment of the judgment reduces the liability of the Cotton Company to the Bank, and accordingly reduces the liability of the president of the corporation, T. W. McDevitt, upon the guaranties, and reduces the financial responsibility principally of West upon his stockholder's liability. There can be no doubt of the liability of West as a stockholder of the Cotton Company as of date December 1, 1920.

If Sears were alive today he would not benefit by the judgment, and being dead his estate is in no different position. The persons principally benefiting by the judgment are West and McDevitt. West is relieved of his stockholder's liability, and McDevitt as guarantor upon the acceptances. West, on December 1, 1920, and at all times prior thereto and subsequent to the organization of the Cotton Company owned 496 of the 500 shares of stock issued and outstanding [Tr. p. 149].

At the time of the sale one share was left in the name of West who continued to act as treasurer and director of the corporation. [Tr. p. 382.] The note [Plaintiff's Exhibit No. 18, Tr. p. 383] given in payment for the transfer of the stock discloses that the 496 shares were pledged as collateral. [Tr. p. 384.] The payment of each of the sight drafts is guaranteed by T. W. McDevitt, president of the Cotton Company. [Tr. p. 220.]

An entirely distinct and perhaps more persuasive answer to this point of plaintiff in error is as follows:

If after December 1, 1920, the Cotton Company was a corporation sole, to-wit: J. B. Sears, then for the same reason prior to December 1, 1920, the Cotton Company was a corporation sole, to-wit: T. J. West.

If the courts will look beyond the corporate entity after December 1, 1920, to prevent a fraud they will do likewise prior to December 1, 1920, to accomplish the same purpose. On December 1, 1920, West, as the corporation sole, had a right of action under the bond

against the plaintiff in error because of the liability then existing and of which he had no knowledge. This is the right of action which was assigned to the defendant in error after the discovery of Sears' lack of fidelity. It was never assigned to Sears and his purchase of the stock (incomplete as it was) did not, and was not intended to, transfer such cause of action to him. The willingness of the courts to look beyond the corporate existence is a shield against, and not a weapon for, the commission of fraud and injustice.

The contention of plaintiff in error though specious is ingenious.

Because of a failure to present this question for consideration to the trial court we repeat the following quotation:

> "While it is the duty of this court to review the action of subordinate courts, justice to those courts requires that their alleged errors should be called directly to their attention, and that their action should not be reversed upon questions which the astuteness of counsel in this court has evolved from the record."
>
> Robinson & Co. v. Belt, 187 U. S. 41, 50.

Point of Plaintiff in Error No. V Answered.

Assignments of error numbers 25 and 30 are by plaintiff in error grouped under the heading

V.

"The court erred in its finding of fact that the control of the Cotton Company did not pass from West to Sears until December 1, 1920."

The Facts Involved Under Point V.

The point presented by counsel for plaintiff in error, as well as the two assignments upon which it is predicated, present for this court's consideration no question of law but merely a consideration of conflicting testimony. Indeed, in the discussion of this point in its brief at pages 95 to 100 the plaintiff in error merely presents for the court's consideration excerpts of conflicting testimony of the witnesses. Naturally, the testimony of witnesses supporting the contention of the plaintiff in error is emphasized and set forth at length, while the conflicting testimony of witnesses produced by the defendant in error are referred to in substance and effect and passed over hurriedly. This date, namely, December 1, 1920, is exceedingly important, in that it fixes the time to which the liability of the plaintiff in error extends. Because of the fact that the testimony is conflicting respecting the date, and of the rule of law that this court will not disturb the finding of the trial court if there is substantial evidence to sustain it we shall quote only the evidence which supports the finding. It is as follows:

Testimony of C. H. Hartke [Tr. pp. 459-462.]

"I recall the occasion of certain certificates of stock * * * being issued in the name of J. B. Sears * * *. I had a conversation with Mr. West in connection with that matter * * * Sears was present. *This conversation took place about the first day of December, 1920.* Mr. West and Mr. Sears * * * asked me what the records showed as to the latest date that the stock appeared in the name of Mr.

West * * * and I told them * * * May 20 * * *. That was practically all of that conversation. *Subsequent to that conversation* I know that certificates for 496 shares of stock were issued in the name of J. B. Sears. I can't say exactly as to when those certificates were issued, but it was sometime *after December 1, 1920* * * *. I put my signature as secretary on those certificates along about December 1, 1920 * * *."

(Referring to the erasures appearing upon the original certificates, the witness testified:)

"Mr. Norsworthy made the erasure, not in my presence, but he acknowledged that he had done it along sometime *after December 1, 1920.* He first had written December 1, or the numerals corresponding to that date in there. I did not see him write the date in there but I saw the figures in there before he had made the correction and I recognized them as his handwriting." [Plaintiff's Exhibit 18, Tr. pp. 383-385.]

This note bearing date December 1, 1920, is the consideration for the 496 shares of stock. In view of the fact that the maker of the note is one T. W. McDevitt and that it was endorsed by Sears to West in consideration for the alleged transfer of stock, the date of the note, namely, December 1, 1920, establishes conclusively that the transfer of the stock could not have taken place prior to that date.

The Law Involved Under Point V.

This court will examine the record when a question of law is presented relating to the evidence, not for

the purpose of weighing conflicting testimony, but only to determine whether there was some evidence, competent and substantial, fairly tending to sustain the finding.

Lancaster v. Collins, 115 U. S. 222, 225;
Chicago & N. W. Ry. Co. v. Ohle, 117 U. S. 123, 129;
Troxell v. D. L. & W. R. R. Co., 227 U. S. 434, 442;
Abrams v. United States, 250 U. S. 616, 619.

When an action at law is tried without a jury by a Federal court and it makes a general or special finding of facts, the Act of Congress forbids reversal by the Appellate Court of that finding or of the judgment based thereon "for any error of fact" (Rev. St. Sec. 1011, U. S. Comp. St. 1913, Sec. 1642, p. 700) and a finding of fact contrary to the weight of the evidence is an error of fact.

Wear v. Imperial Window Glass Co., 224 Fed. 60, 63.

When in an action at law a jury is waived and the court tries an issue of fact and makes a special finding upon which the substantial evidence is conflicting, the losing party may not reverse it by writ of error because it was not sustained by the weight of evidence.

Barnsdall v. Waltemeyer, 142 Fed. 415, 417.

A cursory examination of the contention of counsel for plaintiff in error (Brief pp. 95-100) discloses that there was a sharp conflict of testimony respecting the date when the sale from Sears to West became ef-

fective. The trial court accepted the testimony of the witness Hartke which was competent and substantial.

Point of Plaintiff in Error No. VI Answered.

Assignments of error numbers 2, 20, 23, 27, 28 and 31 are by plaintiff in error grouped under the heading:

VI.

"There was a breach by the Cotton Company of the promissory warranties made to the Bonding Company and given as consideration for the execution of the bond, and of the provisions of the bond in that the Cotton Company's books, accounts, stock and securities were not inspected and audited by T. J. West as warranted."

The Facts Involved Under Point VI.

The representation of the Cotton Company respecting the examination of its books by T. J. West is found in the application for bond, Plaintiff's Exhibit 2, question and answer No. 12 thereof, transcript page 202, reading as follows:

12. (a) At what intervals will applicant's books, accounts, stocks and securities be inspected and audited and verified with funds on hand or in bank? (a) At least once in every.....month. Books checked up each month.

(b) At what intervals and in what manner will outstanding accounts as shown in applicant's books or reports be verified? (b) We have no such accounts.

(d) By whom will above inspections and audits be made? (d) T. J. West, treasurer * * * official capacity.

In the answer to question 12 (a) in the printed form of application used there appeared printed the following:

"(a) At least once in every.....month."

The applicant did not fill in the blank but typed in the answer, reading:

"Books checked up each month." [Tr. p. 144.]

The finding of the court directly in point is finding No. 16 [Tr. pp. 143-146.] This finding is abundantly supported by the evidence appearing in the printed transcript, portions only of which are referred to by counsel for plaintiff in error in its brief, pages 12-16.

For the court's convenience in this matter we set forth the specification of error No. XX in the language of the assignment (Brief pp. 43,44) inserting, however, throughout the specification references to the pages of the printed record where the testimony will be found in support of the finding. It is as follows:

XX.

"There is no evidence to support or justify that part of the finding of fact of the court No. XVI that T. J. West, treasurer of said California Cotton & Factorage Company, 'visited the office of the said California Cotton & Factorage Company semi-monthly [Tr. p. 330] during the term of said bond as herein found and at such times conferred with J. B. Sears respecting the business of said Company [Tr. p. 330] and checked over the books of said Company [Tr. pp. 330, 334, 338] but not in detail at any time examining the cotton account being the purchase and sales cotton ac-

count [Tr. pp. 330, 334, 338] showing the cotton bought and sold and at said times examined the records disclosing the amount of cotton bought, the amount of cotton sold, the number of bales unsold, the entries respecting the hedging of the same, [Tr. pp. 330, 334, 338] and also examined the cash account and the acceptance account [Tr. pp. 337, 338], together with the cotton tickets indicating the number of bales of cotton on hand and compared the same and determined that they corresponded to the acceptances in the plaintiff bank [Tr. pp. 334, 337, 338], and that at such times said T. J. West checked the books of said Company for the purpose of determining the amount of money owing by said Company to said Citizens National Bank [Tr. pp. 338, 339] and examined the statements and books of said Company and did observe the amount of said cotton purchased [Tr. pp. 337, 338], the number of cotton tickets and bales of cotton on hand, [Tr. pp. 337, 338] and examined the ledger books of said Company and the various accounts therein, including the cotton account, and checked the same with the bookkeeper's statement furnished at the end of each month' [Tr. pp. 334,337]; or that

'that said T. J. West checked the accounts of said Company, including the bank account, semi-monthly by said statements rendered by the bookkeeper as herein found' [Tr. pp. 334, 337, 338]."

The finding and evidence appearing in the printed transcript at the pages referred to disclose that twice a month West checked up the books of account of Sears and satisfied himself that they were being properly kept and that the Company was making money. He checked the cotton bought, the cotton sold, the cot-

ton tickets on hand, the acceptance account and the cash account.

The Law Involved Under Point VI.

Counsel for plaintiff in error apparently contends (Br. pp. 101, 111) that the Cotton Company in its application for bond represented that T. J. West, treasurer would at intervals of one month, inspect and audit and verify the applicant's books, accounts, stock and securities with the funds on hand and in the bank. No such representation was made and, as a matter of fact, no such representation is pleaded. We invite the court's attention to the allegation of the special defense [Tr. p. 76]:

"Defendant further avers that pursuant to said application, Exhibit A aforesaid, paragraph 12, subdivisions a and d, the books and accounts of said California Cotton and Factorage Company were to be *'checked up at least once in each month'* by 'T. J. West, treasurer.'"

Then follow the allegations upon information and belief that no audit was made of the books, accounts, stocks and securities of the company nor any inspection, audit or verification of the funds.

As we interpret the application, the California Cotton & Factorage Company did not agree to inspect nor to audit nor to verify the books or accounts or stock or securities with the funds either on hand or in the bank at any stated period, or at all. What it represented would be done was as the Bonding Company pleads, viz: "that the books would be checked up each

month by T. J. West". The plaintiff in error contends that the California Cotton & Factorage Company should, each month, have made such an examination of the books and accounts as would have disclosed Sears' frauds.

A representation that the books and accounts kept by the employee would be examined from time to time in the regular course of business does not mean such a thorough and exhaustive examination as would necessarily discover an irregularity that might exist, however cunningly covered up.

1. U. S. F. & G. Co. v. First Nat. Bank, 233 Ill. 475; 84 N. E. 670, at 673;
2. Title Guarantee & Surety Company v. Nichols, 12 Ariz. 405; 100 Pac. 825 at 830 and 831;
3. Title Guarantee & Surety Company v. Nichols, 224 U. S. 346.

In the case of U. S. F. & G. Co. v. First National Bank, *supra*, the bonding company required the bank to file, prior to the expiration of the bond, a certificate stating that the books and accounts of the employee had been examined from time to time in the regular course of business and had been found correct, and that all moneys handled by him had been accounted for. The filing of such certificate was a condition precedent to the issuance of the renewal bond and the renewal bond was issued on the faith of such certificate of the bank signed by its president. Unknown to the officers of the bank, the employee mentioned in the bond had been guilty of embezzlement at the time

the certificate of the bank president was filed and the renewal certificate issued. Concerning the obligation to examine the books of account, this language is found in the opinion of the court (84 N. E. 673):

> "Appellant insists that the failure of the bank to discover this discrepancy is conclusive proof that no examination was, in fact, made. This conclusion is not warranted by the facts and circumstances in this record. If it be assumed that an examination of the bank's books means only such a thorough and exhaustive examination as would necessarily discover the slightest irregularity that might exist, however cunningly covered up, then, of course, appellant's contention would be sound; but this is manifestly not the meaning of the word 'examination' in the certificates in controversy. *If bank officers are to be held to such a rigid method of examination and supervision over the accounts of their employees there would be but little necessity, if any, for purchasing fidelity insurance.* When a trusted employee conceives a scheme of criminal misappropriation of his employer's money, he, at the same time, insures his plans for covering up his wrongdoings. He has many advantages over his employer, since he knows what the real facts are and is therefore always on his guard to allay suspicion, while the employer is ignorant of the real facts and therefore unsuspecting."

In the case of the Title Guarantee and Surety Co. v. Nichols, *supra,* decided by the Supreme Court of Arizona and afterward affirmed on writ of error from the Supreme Court of the United States, the court

uses the following language in disposing of contentions somewhat analogous to the contentions here made:

> "The principal defense was that the loss was due to the neglect of the employer to supervise the conduct of the employee by making such monthly examinations of his account as it agreed to make or have made." (224 U. S. 349.)
>
> "The obligation in respect to examinations of the employee's accounts is found in the application. The questions propounded by the Surety Company and the employer's answers, so far as relevant, were these:
>
> " 'To whom and how frequently will he account for his handlings of funds and securities? Monthly; to Board of Directors.
>
> " 'What means will you use to ascertain whether his accounts are correct? Examination of books and count of money and securities. How frequently will they be examined? Monthly or oftener. By whom will they be examined? Our auditor.' " (224 U. S. 350.)
>
> "The cashier's embezzlements of money were covered by false entries relating to remittance to the bank's correspondents, whereby the balances in such banks were made to appear much larger than they actually were. The defendant's expert evidence tended to show that if the returned vouchers or the reconciliation reports of such banks had been compared with the ledger accounts, the discrepancy would have appeared. But the cashier was cunning, and he testified to the difficulties which he threw in the way of any effort to verify the books in these particulars." (224 U. S. 352.)

"The mere fact that the examination, if made by a reasonably competent person, failed to discover discrepancies covered up by false entries, or other bookkeeping devices, would not defeat the renewal. The case upon this point went to the jury upon the fact of reasonable examinations and the good faith of the bank in making the representation." (224 U. S. 353.)

The evidence in this case discloses that West checked the books and accounts of the Cotton Company every two weeks [Tr. p. 330], twice as frequently as was represented in the application, and that West, although a man of many years experience in the cotton business [Tr. p. 330], was deceived by Sears, because of the falsification of the accounts as found by the court [Tr. pp. 133, 134], and the misrepresentation of Sears that the Company was making money and that the cotton tickets in its possession represented profit [Tr. pp. 330, 331].

Counsel for plaintiff in error has cited several authorities (Br. pp. 112-125-126) in support of his contention that

"The failure of the Cotton Company to have T. J. West make a monthly examination, audit and check of the books as agreed, releases the Bonding Company from all liability." (Br. 111.)

If West had neglected to make a monthly check of the books the decisions referred to and the quotations therefrom and the comments of counsel would be pertinent to the matter in hand. The error of counsel's contention consists in his having taken for granted that which he set out originally to establish (Point 6,

Br. p. 101), namely, that West did not check the accounts as warranted. The court found, upon abundant evidence, that West checked the books and accounts of the Cotton Company semi-monthly. In the decisions cited by plaintiff in error the court in each instance found as a matter of fact that the warranty in regard to inspections had been violated, for example:

(1) Maryland Casualty Co. v. Bank of England, 2 Fed. (2d) 793, (Br. p. 112) applicant represented that the cash and securities would be examined and compared with the books, accounts and vouchers monthly. The court found that there had been no monthly comparisons.

(2) In U. S. F. & G. Co. v. Downey (Colo.), 88 Pac. 451, 10 L. R. A. (N. S.) 323, (Br. p. 114.) There was represented that the books and accounts would be examined and verified with funds and property on hands and in bank every three months, the facts of the case disclosed that there was no attempt to verify the accounts and that the trustees accepted the figures submitted to them by the employee whose fidelity was assured by the Bonding Company.

(3) In Young v. Pac. Surety Co., 137 Cal. 596. It was represented books and accounts, monies, securities and vouchers would be examined and verified daily. The applicant failed for a period of four days to make such examination and verification, during which time the cashier absconded.

(4) In Hunt v. Fidelity Casualty Co., 99 Fed. 242. The applicant represented that the cash would be com-

pared and verified once a month. A direct verdict for the defendant was based upon the specific ground "that there had been no monthly examination by the assured of the cash and accounts of its agent in compliance with the promise of the assured." (99 Fed. 244.)

(5) In Ellzey v. Mass. Bonding & Ins. Co., 142 La. Ann., column 818, the plaintiff admitted failing to carry out the promise with reference to monthly examination by an auditor or expert accountant.

The other authorities cited by plaintiff in error are to the same effect.

In 10 L. R. A. (N. S.) 323, referred to by counsel for plaintiff in error (Br. p. 114) will be found the following opening statement of the case note published in connection with the Colorado case referred to by plaintiff in error:

> "No hard-and-fast rule can be laid down as to what constitutes a verification of accounts in accordance with the requirements of a fidelity contract, especially in view of the paucity of authority on the question. It would seem, however, that, while it is incumbent upon the obligee, in examining the principals' account, to use all means that are palpably within his reach, as was decided by the foregoing case, an examination such as is due and customary with the obligee in his business, if made in good faith, will be a sufficient compliance with such condition in the contract. This was the conclusion reached in Guarantee Co. of N. A. v. Mechanics' Sav. Bank & T. Co., 26 C. C. A. 146, 47 U. S. App. 91, 80 Fed. 766, Affirming 68 Fed.

459, in which it appeared that the bond in question provided that the acts of the principal therein, a bank teller, should be verified by the finance committee of the bank."

We respectfully submit that the finding of the court, sustained by the evidence as heretofore indicated, shows a *bona fide* and substantial compliance with the terms of the applicant to check the books of Sears monthly.

Heretofore in answer to "Point Number V of Plaintiff in Error" we have cited authorities sustaining the principle that the court will not under the writ of error weigh conflicting testimony, but will confine itself to a determination of whether there was some competent and substantial evidence to sustain the finding. We again refer to these authorities in connection with the finding of the court respecting the monthly examination of the Cotton Company's books by West.

Point of Plaintiff in Error No. VII Answered.

The assignments of error numbers 4 to 18, inclusive, and 21 and 24 are by plaintiff in error grouped under the heading:

VII.

"The Cotton Company had knowledge of the performance by Sears of the acts done by him as secretary and which it is now claimed were dishonest for the reason that the acts done by Sears as expressly plead by plaintiff, were within the scope of his duties as secretary, and were for the exclusive benefit of the Cotton Company in the prosecution of the business for

which it was incorporated. It is not claimed that Sears sought to gain any personal advantage or benefit to himself or to any other person than the Cotton Company.

"The failure of the Cotton Company, having knowledge of the acts of Sears now complained of, to notify the Bonding Company thereof within the time provided in the bond, prevents any right of recovery thereon and estops the Cotton Company from maintaining any action predicated upon the alleged fraudulent acts. In view of this knowledge on the part of the Cotton Company it was an error for the trial court to find that any fraud or deceit was practiced by Sears upon the Cotton Company."

The Facts Involved Under Point VII.

The bond contains the following provision respecting notice [Tr. p. 122]:

"This is executed upon the following express conditions, which are conditions precedent to the right of the employer to recover hereon:

2. "* * * That if the employer become aware of the employee committing any act of fraud or dishonesty * * * the employer shall, within ten days thereafter notify the company * * * and the company shall not be liable for any loss subsequently incurred by the employer through any act of the employee unless the company shall have consented in writing to continue its liability under this bond."

The court found [Tr. pp. 134, 135] that Sears represented to the officers and directors of the Cotton Company that the cash items (deposits) in the bank passbook and the corresponding credits entered upon

the books of account of the Cotton Company represented moneys made and accumulated by Sears in the conduct of the affairs of the Cotton Company and represented to the officers of the plaintiff bank that the Cotton Company still retained, and that he as its secretary had in his custody in the vaults of the Cotton Company, the warehouse receipts surrendered to him, and that the officers of the Cotton Company and the plaintiff bank believed and acted upon such dishonest representations.

The court further found [Tr. pp. 137, 138] that relying entirely upon the deceits practiced upon it by Sears the Cotton Company continued its business subsequent to November 19, 1920, consented to Sears continuing to act as secretary and continuing to administer to its affairs; that it and its officers would not have consented to continuing the business subsequent to November 19, 1920, nor have consented to Sears continuing to act as secretary subsequent to that date or have consented to his conducting any dealings or incurring any indebtedness or contracting any financial obligations in its name or upon its behalf had it or its officers known of the frauds, deceits, dishonesties, wrongful conversions and wilful misapplications, or any of them, practiced upon the Cotton Company and its officers or plaintiff Bank and its officers.

These findings are sustained by an abundance of convincing evidence. Testimony of

(1) T. W. McDevitt (president), Transcript pages 234, 235, 268, 269, 270, 271, 272, 279, 280, 286 288, 291.

(2) John P. Conduit (director), Transcript pages 359-360.

(3) C. H. Hartke (director), Transcript pages 361, 362, 363.

(4) T. J. West (treasurer), Transcript pages 329, 330, 331, 332, 333, 334, 337, 338, 340, 341, 344, 346.

In the brief of plaintiff in error [Tr. pp. 127-131] are many gratuitous statements in direct conflict with the foregoing findings and evidence. The rule of this court (Rule 24) requiring "a reference to the pages of the record" supporting a statement of fact to be discussed, is in all likelihood disregarded by plaintiff in error, not from design, but from necessity.

The Law Involved Under Point VII.

Although a corporation, like any other principal, is ordinarily chargeable with the knowledge of any facts which are known to its agents upon the principle of imputed notice, this presumption does not arise where the acts of the agent constitute a fraud against the principal, and the disclosure of such facts by the agent would be a disclosure of his own fraud and dishonesty, and in such cases the principal is not bound by such acts of the agent unless it has actual notice.

American Surety Co. v. Pauly, 170 U. S. 133;
Henry v. Allen, 151 N. Y. 1;
Benedict v. Arnoux, 154 N. Y. 715;
Kettlewell v. Watson, 21 Ch. Div. 685.

Irrespective of the common law duty of the assured to notify the surety of the frauds of the employee,

and wholly irrespective of the principle of imputed knowledge or any exception thereto, the parties to this bond have by express condition of the same (*contemplating actual notice*) declared the responsibility of the assured in the matter of notice.

Guarantee Company of North America v. Mechanics' Savings Bank & Trust Company, 183 U. S. 402;

First National Bank of Crandon v. U. S. F. & G. Co. of Baltimore, 150 Wis., 601, 137 N. W. 742-745;

Remington v. Fidelity & Deposit Co. of Maryland, 27 Wash. 429, 67 Pac. 989;

Bank of Willow Lakes v. Syverson, 43 S. Dak., 295, 178 N. W. 989.

Imputed Knowledge.

(a) *Statement of the Principle.*

The fraudulent acts of Sears were performed within the line of his employment. It is so alleged in the complaint and established by the proof. We have never contended otherwise. It is only the acts performed by Sears "while in the performance of his duties as secretary in the service of such employer and occurring during the continuance of this bond" that are covered by the terms of the bond. Can the Cotton Company upon application of the principle of imputed knowledge be held to have been familiar with Sears' dishonesties? We think not. We predicate our statement upon the propositions, first that the doctrine of imputed knowledge is based upon the rebuttable

presumption that the agent will disclose his information to the principal, and, second, that the presumption is overcome by a showing that such a disclosure would expose the agent's fraud and defeat the objects thereof.

We do not take issue with the principle as stated in the case cited by counsel for defendant, McKenney v. Ellsworth, 165 Cal. 326 at 329, to the effect that:

> "The familiar rule that the principal is bound by the knowledge of his agent, acquired in the course of the agency *rests upon the presumption* that the agent will communicate to the principal the facts learned by him as it is his duty to do * * *. If the agent is in fact acting for his principal in the transaction, even though he may have an opposing personal interest 'it is his duty, notwithstanding his interest, to communicate to his company (principal), any facts in his possession, material to the transaction, and the law will, therefore, presume *in favor of third persons,* that he made such communication.' "

This decision has been subsequently affirmed by our courts of review. We believe it to be authority for the proposition that the rebuttable presumption supporting the doctrine of imputed knowledge is not overcome by showing that the agent "may have an opposing *personal interest.*" This is not quite the case before the court, and does not quite meet our contention unless it can be said that *personal interest* on the part of the agent is the same as *fraud* on the part of the agent.

In the Ellsworth case (165 Cal. 326) a bank president who had actual control of its affairs, and who personally directed the discount by it of a promissory note belonging to himself, had failed to endorse a payment thereon. In an action by the bank upon the note the court declared that the maker was entitled to show the partial payment, the bank being held to have notice of the payment notwithstanding the personal interest of the president therein involved. There were no charges of fraud or deceit involved and such elements did not enter into the considerations of the court.

In support of our contention of the rule, as we have stated it, we rely upon:

1. American Surety Company v. Pauly, 170 U. S. 133.

> "Ordinarily a corporation, like any other principal, is chargeable with the knowledge of any facts which are known to its agents; but in this case all these transactions, if there were any transactions of a *fraudulent and dishonest character* on the part of the cashier, were transactions for the benefit of Collins, and he was a *participator in the fraud*, and under those circumstances the law *does not infer* that the agent or the officer will communicate the fact to his principal, the corporation, and under such circumstances the corporation *is not bound* by his knowledge. So this defense melts away and there is nothing of it whatever." (Page 150.)

Sears was interested in the perpetration of the frauds committed by him in the sense that from the

profits of the corporation, if any, he was entitled to twenty-five per cent thereof, with a five thousand dollar minimum guarantee. [Tr. p. 199.]

Further quoting from the Pauly case:

> "*The presumption* that the agent informed his principal of that which his duty and the interest of his principal required him to communicate, *does not arise* where the agent acts or makes declarations not in execution of any duty that he owes to the principal, nor within any authority possessed by him, but to subserve simply his own personal ends or to commit some fraud against the principal. In such cases the principal is not bound by the acts or declarations of the agent unless it be proved that he had at the time *actual notice* of them, or having received notice of them, failed to disavow what was assumed to be said and done in his behalf." (Pages 156 and 157.)

Although Sears' acts were within the course of his employment as secretary of the Cotton Company, they were in the particulars alleged in the complaint dishonestly and fraudulently performed, and were performed to carry into effect a dishonest scheme conceived and executed by him which would have failed in its inception had his principals known of his deceits and duplicities.

2. Henry v. Allen, 151 N. Y. 1.

> "The general rule that notice to the agent, while acting within the scope of his authority and in regard to a matter over which his authority extends, is notice to the principal, *rests upon the duty* of disclosure by the former to the latter of

all the material facts coming to his knowledge with reference to the subject of his agency and upon the *presumption that he has discharged* that duty. (Citing authorities.) This presumption, however, does not always arise, for there are *several exceptions* well recognized by the authorities. Thus, when the agent has no legal right to disclose a fact to his principal, or he is *engaged* in a *scheme to defraud* his principal, the *presumption does not prevail,* because he cannot in reason be presumed to have disclosed that which it was his duty to keep secret, or that which would *expose and defeat his fraudulent purpose.* (Citing authorities.) As Mr. Pomeroy says in his work on Equity Jurisprudence: 'When an agent or attorney has in the course of his employment *been guilty* of an *actual fraud,* contrived and carried out for *his own benefit,* by which he intended to defraud, and did defraud, his own principal or client, as well as perhaps the other party, and the *very perpetration* of such fraud *involved the necessity of his conceding the facts* from his own client, then, under such circumstances, the prinpal is not charged with constructive notice of facts known by the attorney, and thus fraudulently concealed. In other words, if, in the course of the *same transaction* in which he is employed, the agent commits an independent fraud for his own benefit, and designedly against his principal, *and it is essential to the very existence* or possibility of such fraud that he should conceal the real facts from his principal, *then the ordinary presumption* of a communication from the agent to his principal *fails; on the contrary,* a presumption arises that no communication was made, and conse-

quently the principal is not affected with constructive notice.' (Section 675)." (Pages 9 and 10.)

3. Benedict v. Arnoux, 154 N. Y. 715, 728.

"It affirmatively appears in the case that Booth knew nothing of the transaction. It is claimed, however, that the knowledge of his agent is *imputable* to him. This is true to a limited extent; so long as the agent acts within the scope of his employment *in good faith*, for the interest of his principal, he is presumed to have disclosed to his principal all the facts that come to his knowledge as agent; but just as soon as the agent *forms the purpose of dealing with his principal's property for his own benefit and advantage*, or for the benefit and advantage of other persons who are opposed in interest, he ceases, in fact, to be an agent *acting in good faith* for the interest of his principal, and his action thereafter based upon such purpose is deemed to be in fraud of the rights of his principal, and the presumption that he has disclosed all the facts that have come to his knowledge no longer prevails. *The citation of authorities to sustain this proposition* is hardly necessary, but it may not be out of place to call attention to the case of Henry v. Allen." (Page 728.)

4. Kettlewell v. Watson, 21 Chancery Division 685.

"There is another principle which undoubtedly is well established, and is an *exception* from the doctrine of imputed notice, that which is familiarly known by reference to the case of Kennedy v. Green. There it was held that the presumption which arises from the duty of the agent to com-

> municate what he knows to his principal, *may be repelled* by showing that, whilst he was acting as agent, he was also acting in another character, viz, *as a party to a scheme or design of fraud,* and that the knowledge which he attained was attained by him in the latter character, and that therefore there is no ground on which you can presume that the duty of an agent was performed by the person who filled that double character. That I understand to be the principle of that class of cases." (Page 707.)

This exception to the general principle applies as well to corporate principals as to personal principals. It was a *corporate principal* that was involved in the *Pauly* case, and the case of *Henry v. Allen.*

As we understand, counsel for plaintiff in error contends that whenever the agent possessed of the knowledge is a director of a corporation or general manager of a corporation, then he is the corporation and the corporation as such has the knowledge. We take issue with counsel upon this proposition, and assert that there is no authority to sustain the contention and declare that the authorities we have cited, particularly the Pauly case, is to the contrary. In the Pauly case, the president, Collins, and the cashier, O'Brien, were the parties perpetrating the fraud. They were the chief executive officers of the bank, and we think it reasonable and fair to argue that it would be difficult ordinarily to experience an instance in the commercial world where the officers of a corporation could be said to be closer or less far removed from the fictitious corporate entity than the president and cashier of a

bank in a community of moderate size. The entire fraudulent conduct of O'Brien and Collins in making the false and dishonest entries of credit to the account of Collins were performed as cashier and president of the Bank. The Bank as a corporation, however, did not know it, did not participate in a fraud upon itself and the Bonding Company was required to indemnify the Bank for its loss (so far as the liability thereunder would do so).

In its final analysis, the doctrine of imputed knowledge merely furnishes a legal theory upon which a principal may be held. The courts do not declare that the principal had actual knowledge of the facts; they declare merely that the principal's liability is the same as though it had actual knowledge.

(b) *Application of the Principle.*

Whether the principle of imputed knowledge and the exception thereto is correctly stated by counsel for the plaintiff in error or by ourselves, or by neither of us, we contend it is of no consequence in the matter now before the court for the reason that the Bonding Company and the Cotton Company entered into a contract defining the duty of Cotton Company concerning any act of fraud or dishonesty of Sears. Let it be assumed for sake of argument that the doctrine of imputed knowledge applies in this case without the limitation of the exception as we have contended. Still the Bonding Company cannot escape liability if they are otherwise responsible for the reason that they have specifically agreed with the Cotton Company

that it is only when the Cotton Company has actual knowledge of the facts constituting fraud or dishonesty that it is required to notify the insurer. Quoting from the bond:

"This bond is executed upon the following express conditions; which are conditions precedent to the right of the Employer to recover hereunder;

2. * * *, that if the Employer *become aware* of the Employee committing any act of fraud or dishonestly, * * * the employer shall * * * notify the company, * * *, and the company shall not be liable for any loss subsequently incurred * * * unless the company shall have consented * * * to continue its liability. * * *." [Tr. p. 206.]

Irrespective of the common law duty of the assured to notify the surety of the frauds of the employee, and wholly irrespective of the principle of imputed knowledge or any exception thereto, the parties to this bond have by express condition of the same declared the responsibility of the assured thereunder. In support of our contention in this particular, we invite the court's attention to the case of Guarantee Company of North America v. Mechanics' Savings Bank & Trust Company, 183 U. S., 402. This was a suit in equity to enforce an account on bonds of fidelity insurance, one covering the employee as teller and collector, and the other as cashier of the bank.

> "In addition to the provisions already mentioned, it was agreed 'that the employer shall at once notify the company, on his *becoming aware of the said employee being engaged in speculation*

or gambling, or indulging in any disreputable or unlawful habits or pursuits.'" (Page 417.)

"The evidence showed that in the summer or fall of 1892. the cashier of the bank was told that the teller was part owner in a concern engaged in speculative business; he at once informed the president of the bank; and also called Schardt's (employee covered by the bond) attention to the matter, who admitted that he had once been engaged in such a concern, but said he had sold out, and also that he had speculated to some extent, but had ceased to do so." (Page 418.)

It also appears that the bank received an anonymous letter that Schardt was speculating. This matter came to the attention of the president of the bank, and through a second director, to a third director and member of the Finance Committee. It also appears that the directors had the matter up with Schardt, who admitted that he had been, but denied that he then was engaged in stock speculation. The court asks:

"In these circumstances was it the duty of the bank to notify the company of what it had heard?" (Page 418.)

The Pauly case is then referred to and the doctrine quoted to the effect that where a bond is fairly susceptible of two constructions, one favorable to the assured, and the other to the surety company, the former should be adopted. The court proceeds:

"But this rule cannot be availed of to refine away terms of a contract expressed with sufficient clearness to convey the plain meaning of the

parties, and embodying requirements compliance with which is made the condition to liability thereon.

"Whatever the common law duty on the part of the employer to notify the guarantor of the fraud or dishonesty of the employee, whose fidelity is guaranteed, the parties to this contract undertook to declare the duty of the bank to the company in *certain specified particulars.* It required that the employee should not have been guilty of previous default or dereliction *within the knowledge* of the employer. It provided for notification of any act of the employee which might involve a loss without unreasonable delay after the occurrence of the act came *to the knowledge* of the employer. And it required immediate notification on the employer *becoming aware of the employee being engaged in speculation or gambling.*" (Page 419.)

It is important to note that the words *"becoming aware"* hereinbefore italicized in the opinion of the Supreme Court are the identical words used in the bond under consideration in the provision hereinbefore quoted. The court then calls attention to the language of the Pauly case requiring "notice of any act on the part of the employee which may involve a loss for which the company is responsible" and to the holding that this clause did not require notice when the suspicion of the bank was aroused. Then this significant statement appears in the opinion.

"But the bond before us not only contained that clause but the clause under consideration, which

was a different and additional clause *intended to secure the safety of prevention* through timely warning."

"It seems to us that the obvious meaning of *'becoming aware,'* as used in this bond is 'to be informed of,' or to be apprised of' or *'to be put on one's guard in respect to'* and that no other meaning is equally admissible under the terms of the instrument. These are the definitions of the lexicographers, distinctly deducible from the derivation of the word *'aware',* and that is the sense in which they are here employed. * * *. Our understanding of the provision is that what the company stipulated for was prompt notification *of information by the bank* in regard to speculation or gambling on the part of the employe." (Page 420.)

Reference is then made to language appearing in the opinion of the Circuit Court, and in the opinion of the Circuit Court of Appeals relating to the question of bad faith or bad judgment on the part of the bank officials. The court then says:

"The company's defense did not rest on the duty of diligence growing out of the relation of the parties, but *on the breach of one of the stipulations entered into between them.* The question was not merely whether the conduct of the bank *was contrary to the nature of the contract, but whether it was not contrary to its terms.*" (Pages 421-422.)

"The truth is that in spite of strict supervision and the pursuit of the best systems of keeping accounts, there is always a risk of defalcation. The

prevention of defaults or their detection at the earliest possible moment are of even more vital importance to financial institutions than to the guarantors of the fidelity of their employees. The provisions intended to protect the company in this case were not in themselves unreasonable and so far as they operated to compel the bank to exercise due supervision and examination, and due vigilance, were consistent with sound public policy. We think it was the duty of this bank to have made prompt investigation, or at all events to have notified the company at once of the information that it had, and we decline to hold that the bank's misplaced confidence in Schardt affords sufficient ground for enforcing the liability of the surety company on the theory of good faith.

"Our conclusion is that the failure of the bank in the particulars adverted to defeats a recovery on the teller's bond for defalcation *after information of Schardt being engaged in speculation was received.*" (Page 422.)

First National Bank of Crandon v, U. S. Fidelity & Guaranty Company of Baltimore, 150 Wis. 601; 137 N. W. 742, at 745, is authority for the proposition that the notice or information which the employer must immediately indicate to the insurer under penalty of releasing the insurer for failure so to do is *actual knowledge* and does not include constructive notice. Points 3 and 4 found discussed upon page 745 of the 137 N. W. Reporter, contain clear declarations of this principle. For example, it is said:

"The finding of the Circuit Court negatives *actual knowledge* of the practice of kiting checks after the time stated. It is true there is evidence in the case from which the court might have found that such knowledge existed, but the officers of the bank denied having such knowledge, and a finding in accordance with their testimony is fairly supported by the evidence. * * * The language of the bond is that the employer would notify the defendant of certain facts if the same should 'come to the knowledge of the employer.' *We interpret this provision of the bond to mean actual knowledge and not mere constructive notice,* which is a very different thing from knowledge, although in some cases its legal effect may be the same. The bond did not require the plaintiff to notify the defendant of matters of which it had knowledge and *also of matters of which it might have had knowledge had its officers made a critical examination of its books from time to time.*" (Page 745.)

There was no possibility of the Cotton Company acquiring actual knowledge of the information possessed by Sears upon the theory of imputed knowledge. In other words a holding to the effect that the knowledge of Sears is imputed to the corporation, which in turn, under penalty of forfeiture of the coverage of the bond, must have conveyed the information to the Surety Company, is to declare that the Cotton Company was required to inform the Bonding Company of matters never coming to the knowledge of the Cotton Company. To state the matter in a different manner, the assured would be deprived of the benefit of the

bond for failure to do that which was humanly impossible, namely, to impart information which it did not itself possess, and in violation of the express provision of the bond applying to actual knowledge.

The case of Remington v. Fidelity & Deposit Company of Maryland, 27 Wash. 429; 67 Pac. 989, was an action against an insurer to recover upon a fidelity bond of the cashier of the plaintiff. The bond contained a provision requiring the employer to immediately notify the Insurance Company of any default on the part of the employee. It was contended by the defendant that there had been a breach of this condition. Respecting this defense the court says:

> "Bonds of this character are, in their nature, insurance contracts, to indemnify the employer against the dishonesty of employees. They are issued for profit, and the same rules of construction must apply thereto as apply to other insurance contracts. * * * The provisions in the contract above quoted are for the protection of the insurance company. They were not intended to avoid an existing liability under the contract, or as a means of defeating recovery thereon, but only to prevent further liability *after discovery* of dishonesty by the employer. For such purpose the provisions are reasonable and will be maintained, but *if they are to be considered as a shield* to avoid a liability legally and rightfully due, or to avoid a contract properly, made, they are a fraud upon the rights of the insured, and cannot be upheld." (Page 991.)

It is our contention that the doctrine of imputed knowledge has no application because of the fact that

"the parties to the contract undertook to declare the duty of the (employer) to the (Bonding) Company in certain specified particulars."

Guarantee Co. v. Mechanics' Bank & Trust Co., 183 U. S. 402, at 419.

Further in this connection we quote from a decision of the Supreme Court of South Dakota:

> "The application and policy constitute the entire contract between the bank and the company, and the courts are without power to interpolate into it conditions wholly foreign to its express or implied provisions." (Bank of Willow Lakes v. Syverson, 43 So. Dak. 295, 178 N. W. 989, at 991.)

Conclusion.

The motion to strike the bill of exceptions is well taken. There is no attempt made to set out any "very extraordinary circumstances" justifying the trial court in settling and certifying the bill after the expiration of the term. The trial court's action is attempted to be justified upon the doctrine of estoppel. (Br. pp. 30, 31). In the brief of plaintiff in error no mention is made of the leading and recent case of Exporters etc. Inc. v. Butterworth-Judson Co., 258 U. S. 365, and the many more recent decisions pointing it out as the last authoritative word upon this subject. Had counsel for plaintiff in error been familiar with this decision they would not have relied upon the doctrine of estoppel.

Because of the failure to obtain a ruling or request a ruling upon the motion of plaintiff in error for a declaration of law and special findings in its favor

[Tr. p. 466], and because of a failure to save an exception to a ruling or a failure to rule upon such motion only two questions are open to review under the writ.

Of these the first—

The alleged insufficiency of the complaint—is not argued or presented here for review. The sufficiency of the complaint is apparent upon a casual examination, as must be conceded because of the failure of plaintiff in error to contend to the contrary.

In a consideration of the second, viz:

The sufficiency of the findings to sustain the judgment—we are met at the outset with the problem as to whether this question is raised by any proper assignment of error. Unless the question is presented by assignment No. XXVII [Tr. p. 535] it is not presented at all. In this brief we have proceeded upon the theory that the question is properly and adequately raised by this assignment.

That the findings support the judgment we believe will be manifest to the court long before the end of this exceedingly lengthy brief is reached by those who are compelled to examine it.

For the consideration of the court we urge the granting of the motion to strike the bill of exceptions and an affirmance of the judgment.

Respectfully submitted,

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